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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549**

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**FORM 10-Q**

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(Mark One)

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2020

OR

- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 001-36439

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**PRECIPIO, INC.**

(Exact name of registrant as specified in its charter)

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**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**91-1789357**  
(I.R.S. Employer  
Identification No.)

**4 Science Park, New Haven, CT**  
(Address of principal executive offices)

**06511**  
(Zip Code)

**(203) 787-7888**

(Registrant's telephone number, including area code)

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Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, \$0.01 par value per share	PRPO	The Nasdaq Stock Market LLC

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).

Yes  X  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer   
Non-accelerated filer  Smaller reporting company   
Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  
Yes  No

As of November 11, 2020, the number of shares of common stock outstanding was 17,226,916.

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## PRECIPIO, INC. AND SUBSIDIARIES

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**PART 1. FINANCIAL INFORMATION**

**Item 1. Condensed Consolidated Financial Statements**

**PRECIPIO, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(Dollars in thousands, except share data)

	September 30, 2020	December 31, 2019
	(unaudited)	
<b>ASSETS</b>		
<b>CURRENT ASSETS:</b>		
Cash	\$ 2,158	\$ 848
Accounts receivable, net	1,086	574
Inventories	280	184
Other current assets	444	272
Total current assets	3,968	1,878
<b>PROPERTY AND EQUIPMENT, NET</b>	460	431
<b>OTHER ASSETS:</b>		

Operating lease right-of-use assets	358	519
Intangibles, net	15,904	16,658
Other assets	27	25
<b>Total assets</b>	<b>\$ 20,717</b>	<b>\$ 19,511</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>CURRENT LIABILITIES:</b>		
Current maturities of long-term debt, less debt issuance costs	\$ 530	\$ 321
Current maturities of convertible notes, less debt discounts and debt issuance costs	—	142
Current maturities of finance lease liabilities	37	52
Current maturities of operating lease liabilities	219	209
Accounts payable	1,829	1,936
Accrued expenses	1,804	1,639
Deferred revenue	48	35
<b>Total current liabilities</b>	<b>4,467</b>	<b>4,334</b>
<b>LONG TERM LIABILITIES:</b>		
Long-term debt, less current maturities and debt issuance costs	500	198
Finance lease liabilities, less current maturities	108	119
Operating lease liabilities, less current maturities	150	317
Common stock warrant liabilities	1,631	1,338
<b>Total liabilities</b>	<b>6,856</b>	<b>6,306</b>
<b>COMMITMENTS AND CONTINGENCIES (Note 6)</b>		
<b>STOCKHOLDERS' EQUITY:</b>		
Preferred stock - \$0.01 par value, 15,000,000 shares authorized at September 30, 2020 and December 31, 2019, 47 shares issued and outstanding at September 30, 2020 and December 31, 2019, liquidation preference of \$288 at September 30, 2020	—	—
Common stock, \$0.01 par value, 150,000,000 shares authorized at September 30, 2020 and December 31, 2019, 16,676,916 and 7,898,117 shares issued and outstanding at September 30, 2020 and December 31, 2019, respectively	167	79
Additional paid-in capital	83,362	74,065
Accumulated deficit	(69,695)	(60,939)
<b>Total Precipio, Inc. stockholders' equity</b>	<b>13,834</b>	<b>13,205</b>
Noncontrolling interest in joint venture	27	—
<b>Total stockholders' equity</b>	<b>13,861</b>	<b>13,205</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 20,717</b>	<b>\$ 19,511</b>

See notes to unaudited condensed consolidated financial statements.

**(Dollars in thousands, except per share data)**  
**(unaudited)**

	<u>Three Months Ended September 30,</u>		<u>Nine Months Ended September 30,</u>	
	<u>2020</u>	<u>2019</u>	<u>2020</u>	<u>2019</u>
<b>SALES:</b>				
Service revenue, net	\$ 1,998	\$ 1,020	\$ 5,072	\$ 3,125
Other	51	26	104	37
Revenue, net of contractual allowances and adjustments	2,049	1,046	5,176	3,162
less allowance for doubtful accounts	(422)	(262)	(1,025)	(723)
Net sales	1,627	784	4,151	2,439
<b>COST OF SALES:</b>				
Cost of service revenue	1,244	756	3,472	2,201
Other	6	–	6	–
Total cost of sales	1,250	756	3,478	2,201
Gross profit	377	28	673	238
<b>OPERATING EXPENSES:</b>				
Operating expenses	2,809	2,391	7,567	6,955
<b>OPERATING LOSS</b>	(2,432)	(2,363)	(6,894)	(6,717)
<b>OTHER (EXPENSE) INCOME:</b>				
Interest expense, net	(3)	(97)	(470)	(298)
Warrant revaluation	(857)	563	(293)	(19)
Loss on modification of warrants	–	–	–	(1,128)
Derivative revaluation	–	–	–	(415)
Gain on settlement of liability, net	–	–	–	1,251
Loss on extinguishment of debt	–	–	(1,225)	–
Loss on litigation	–	–	–	(266)
Loss on issuance of convertible notes	–	–	–	(1,870)
Other income	–	–	153	–
Total other (expense) income	(860)	466	(1,835)	(2,745)
<b>LOSS BEFORE INCOME TAXES</b>	(3,292)	(1,897)	(8,729)	(9,462)
INCOME TAX BENEFIT	–	–	–	–
<b>NET LOSS</b>	(3,292)	(1,897)	(8,729)	(9,462)
Less: Net income attributable to noncontrolling interest in joint venture	(10)	–	(27)	–
Deemed dividends related to beneficial conversion feature of preferred stock and fair value of warrant down round features	–	–	(3,344)	–
<b>NET LOSS ATTRIBUTABLE TO PRECIPIO, INC. COMMON STOCKHOLDERS</b>	\$ (3,302)	\$ (1,897)	\$ (12,100)	\$ (9,462)
<b>BASIC AND DILUTED LOSS PER COMMON SHARE</b>	\$ (0.21)	\$ (0.31)	\$ (1.01)	\$ (1.85)
<b>BASIC AND DILUTED WEIGHTED-AVERAGE SHARES OF COMMON STOCK OUTSTANDING</b>	16,007,025	6,186,119	11,925,642	5,104,397

See notes to unaudited condensed consolidated financial statements.

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**PRECIPIO, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**  
(Dollars in thousands)  
(unaudited)

	For the Three Months Ended September 30, 2020								
	Preferred Stock		Common Stock		Additional		Total	Noncontrolling	
	Outstanding Shares	Par Value	Outstanding Shares	Par Value	Paid-in Capital	Accumulated Deficit		Precipio, Inc.	Interest in Joint Venture
Balance, July 1, 2020	47	\$ —	14,616,916	\$ 146	\$ 78,857	\$ (66,393)	\$ 12,610	\$ 17	\$ 12,627
Net (loss) income	—	—	—	—	—	(3,302)	(3,302)	10	(3,292)
Issuance of common stock in connection with purchase agreements	—	—	2,060,000	21	4,293	—	4,314	—	4,314
Stock-based compensation	—	—	—	—	212	—	212	—	212
Balance, September 30, 2020	<u>47</u>	<u>\$ —</u>	<u>16,676,916</u>	<u>\$ 167</u>	<u>\$ 83,362</u>	<u>\$ (69,695)</u>	<u>\$ 13,834</u>	<u>\$ 27</u>	<u>\$ 13,861</u>

	For the Nine Months Ended September 30, 2020								
	Preferred Stock		Common Stock		Additional		Total	Noncontrolling	
	Outstanding Shares	Par Value	Outstanding Shares	Par Value	Paid-in Capital	Accumulated Deficit		Precipio, Inc.	Interest in Joint Venture
Balance, January 1, 2020	47	\$ —	7,898,117	\$ 79	\$ 74,065	\$ (60,939)	\$ 13,205	\$ —	\$ 13,205
Net (loss) income	—	—	—	—	—	(8,756)	(8,756)	27	(8,729)
Conversion of convertible notes into common stock	—	—	3,908,145	39	2,137	—	2,176	—	2,176
Issuance of common stock in connection with purchase agreements	—	—	4,870,654	49	6,872	—	6,921	—	6,921
Write-off debt premiums (net of debt discounts) in conjunction with convertible note conversions	—	—	—	—	270	—	270	—	270
Write-off beneficial conversion feature in conjunction with convertible note extinguishment	—	—	—	—	(523)	—	(523)	—	(523)
Stock-based compensation	—	—	—	—	541	—	541	—	541
Balance, September 30, 2020	<u>47</u>	<u>\$ —</u>	<u>16,676,916</u>	<u>\$ 167</u>	<u>\$ 83,362</u>	<u>\$ (69,695)</u>	<u>\$ 13,834</u>	<u>\$ 27</u>	<u>\$ 13,861</u>

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**PRECIPIO, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY - CONTINUED**  
(Dollars in thousands)  
(unaudited)

	For the Three Months Ended September 30, 2019								
	Preferred Stock		Common Stock		Additional Paid-in Capital	Accumulated Deficit	Total Precipio, Inc.	Noncontrolling	
	Outstanding Shares	Par Value	Outstanding Shares	Par Value				Interest in Joint Venture	Total
Balance, July 1, 2019	47	\$ —	5,993,369	\$ 60	\$ 69,428	\$ (55,261)	\$ 14,227	\$ —	\$14,227
Net loss	—	—	—	—	—	(1,897)	(1,897)	—	(1,897)
Conversion of convertible notes into common stock	—	—	52,748	—	118	—	118	—	118
Issuance of common stock in connection with purchase agreements	—	—	1,090,000	11	2,750	—	2,761	—	2,761
Write-off debt discounts (net of debt premiums) in conjunction with convertible note conversions	—	—	—	—	(63)	—	(63)	—	(63)
Stock-based compensation	—	—	—	—	148	—	148	—	148
Balance, September 30, 2019	<u>47</u>	<u>\$ —</u>	<u>7,136,117</u>	<u>\$ 71</u>	<u>\$ 72,381</u>	<u>\$ (57,158)</u>	<u>\$ 15,294</u>	<u>\$ —</u>	<u>\$15,294</u>
	For the Nine Months Ended September 30, 2019								
	Preferred Stock		Common Stock		Additional Paid-in Capital	Accumulated Deficit	Total Precipio, Inc.	Noncontrolling	
	Outstanding Shares	Par Value	Outstanding Shares	Par Value				Interest in Joint Venture	Total
Balance, January 1, 2019	47	\$ —	2,298,738	\$ 23	\$ 53,796	\$ (47,696)	\$ 6,123	\$ —	\$ 6,123
Net loss	—	—	—	—	—	(9,462)	(9,462)	—	(9,462)

Conversion of convertible notes into common stock	—	—	2,439,173	24	7,366	—	7,390	—	7,390
Issuance of common stock in connection with purchase agreements	—	—	2,088,077	21	5,150	—	5,171	—	5,171
Issuance of common stock upon exercise of warrants	—	—	310,200	3	1,572	—	1,575	—	1,575
Write-off warrant liability in conjunction with warrant exercises	—	—	—	—	2,364	—	2,364	—	2,364
Beneficial conversion feature on issuance of convertible notes	—	—	—	—	1,792	—	1,792	—	1,792
Write-off debt discounts (net of debt premiums) in conjunction with convertible note conversions	—	—	—	—	(590)	—	(590)	—	(590)
Write-off debt derivative liability in conjunction with convertible note conversions	—	—	—	—	477	—	477	—	477
Stock-based compensation	—	—	—	—	455	—	455	—	455
Payment of fractional common shares in conjunction with reverse stock split	—	—	(71)	—	(1)	—	(1)	—	(1)
Balance, September 30, 2019	<u>47</u>	<u>\$ —</u>	<u>7,136,117</u>	<u>\$ 71</u>	<u>\$ 72,381</u>	<u>\$ (57,158)</u>	<u>\$ 15,294</u>	<u>\$ —</u>	<u>\$15,294</u>

See notes to unaudited condensed consolidated financial statements

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**PRECIPIO, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Dollars in thousands)  
(unaudited)

	<u>Nine Months Ended September 30,</u>	
	<u>2020</u>	<u>2019</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net loss	\$ (8,729)	\$ (9,462)
Adjustments to reconcile net loss to net cash flows used in operating activities:		
Depreciation and amortization	829	838
Amortization of operating lease right-of-use asset	161	176
Amortization of finance lease right-of-use asset	38	46
Amortization (accretion) of deferred financing costs, debt discounts and debt premiums	319	(8)
Gain on settlement of liability, net	—	(1,251)
Loss on litigation	—	266



Loss on issuance of convertible notes	—	1,870
Loss on extinguishment of convertible notes	1,225	—
Stock-based compensation	541	455
Provision for losses on doubtful accounts	1,025	724
Warrant revaluation	293	19
Loss on modification of warrants	—	1,128
Derivative revaluation	—	415
Gain from sale of fixed asset	(55)	—
<b>Changes in operating assets and liabilities:</b>		
Accounts receivable	(1,537)	(727)
Inventories	(96)	15
Other assets	(151)	302
Accounts payable	(107)	(1,624)
Operating lease liabilities	(157)	(170)
Accrued expenses and other liabilities	418	(13)
Net cash used in operating activities	(5,983)	(7,001)
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Purchase of property and equipment	(121)	(49)
Proceeds from sale of fixed asset	55	—
Net cash used in investing activities	(66)	(49)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Principal payments on finance lease obligations	(47)	(44)
Payment of deferred financing costs	—	(120)
Payment of fractional common shares in conjunction with reverse stock split	—	(1)
Issuance of common stock, net of issuance costs	6,921	5,171
Proceeds from exercise of warrants	—	1,575
Proceeds from long-term debt	787	—
Proceeds from convertible notes	—	2,150
Principal payments on convertible notes	—	(50)
Principal payments on long-term debt	(302)	(329)
Net cash flows provided by financing activities	7,359	8,352
<b>NET CHANGE IN CASH</b>	1,310	1,302
<b>CASH AT BEGINNING OF PERIOD</b>	848	381
<b>CASH AT END OF PERIOD</b>	<u>\$ 2,158</u>	<u>\$ 1,683</u>

See notes to unaudited condensed consolidated financial statements.

**PRECIPIO, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS- CONTINUED**  
(Dollars in thousands)  
(unaudited)

	<u>Nine Months Ended September 30,</u>	
	<u>2020</u>	<u>2019</u>
<b>SUPPLEMENTAL CASH FLOW INFORMATION</b>		
Cash paid during the period for interest	\$ 25	\$ 27
<b>SUPPLEMENTAL DISCLOSURE OF CONSULTING SERVICES OR ANY OTHER NON-CASH COMMON STOCK RELATED ACTIVITY</b>		
Purchases of equipment financed through accounts payable	—	4
Equipment financed through finance lease obligations	21	23
Discount of 9% on issuance of convertible bridge notes	—	188
Conversion of convertible debt, plus interest, into common stock	2,176	7,390
Beneficial conversion feature on issuance of convertible notes	—	1,792
Initial valuation of derivative liability recorded in conjunction with issuance of convertible notes	—	1,858
Liabilities exchanged for convertible notes	—	2,150
Prepaid insurance financed with loan	23	434
Write-off of beneficial conversion feature in conjunction with convertible note extinguishment	523	—
Right-of-use assets obtained in exchange for lease obligations	—	750
Write-off warrant liability in conjunction with warrant exercises	—	2,364
Write-off of debt discounts (net debt premiums) in conjunction with convertible note conversions	(270)	590
Write-off of derivative liability in conjunction with convertible note conversions	—	477

See notes to unaudited condensed consolidated financial statements.

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**PRECIPIO, INC. AND SUBSIDIARIES**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
For the Three and Nine Months Ended September 30, 2020 and 2019

**1. BUSINESS DESCRIPTION**

*Business Description.*

Precipio, Inc., and its subsidiaries, (collectively, “we”, “us”, “our”, the “Company” or “Precipio”) is a cancer diagnostics company providing diagnostic products and services to the oncology market. We have built and continue to develop a platform designed to eradicate the problem of misdiagnosis by harnessing the intellect, expertise and technologies developed within academic institutions, and delivering quality diagnostic information to physicians and their patients worldwide. We operate a cancer diagnostic laboratory located in New Haven, Connecticut and have partnered with various academic institutions to capture the expertise, experience and technologies developed within academia to provide a better standard of cancer diagnostics and aim to solve the growing problem of cancer misdiagnosis. We also operate a research and development facility in Omaha, Nebraska which focuses on development of various technologies, among them IV-Cell, HemeScreen and ICE-COLD-PCR, or ICP, the patented technology described further below, which we exclusively licensed from Dana-Farber Cancer Institute, Inc., or Dana-Farber, at Harvard University. The research and development center focuses on the development of these technologies, which we believe will enable us to commercialize these and other technologies developed with our current and future academic partners. The facility in Omaha was also recently certified as a CLIA and CAP facility, and we have begun bringing in house several molecular tests that the Company had previously referred out to other laboratories. Our platform also connects patients, physicians and diagnostic experts residing within academic institutions.

#### *Joint Venture.*

In April 2020, the Company formed a joint venture with Poplar Healthcare PLLC (“Poplar”), which we refer to as the “Joint Venture”. The Joint Venture was formed by the Limited Liability Company Agreement of Precipio Oncometrix LLC, a Delaware limited liability company (“POC”), which was entered into as of April 11, 2020 (the “Effective Date”), by and among POC, Poplar, and Precipio SPV Inc. (“Precipio SPV”), a newly formed subsidiary of the Company, together with such other persons who from time to time become party to the Limited Liability Company Agreement by executing a counterpart signature page in accordance with the terms hereof. POC was formed as a limited liability company on April 2, 2020 in accordance with the statutes and laws of the State of Delaware relating to limited liability companies, including, without limitation, the Delaware Act, by the filing of a Certificate of Formation with the office of the Secretary of State of the State of Delaware. Precipio SPV was incorporated in the State of Delaware on March 10, 2020 for the sole purpose of being a party to the Joint Venture.

Under the terms of the Joint Venture, Precipio SPV has a 49% ownership interest in the Joint Venture, with Poplar having a 51 % ownership. Pursuant to the Limited Liability Company Agreement, Poplar, at any time, has the right to require Precipio SPV to purchase all, but not less than all, of Poplar’s shares in the Joint Venture (the “Poplar Put Right”). The purchase price for Poplar’s shares shall be \$1.00 per share, or fifty-one dollars, and Precipio SPV would, therefore, become the sole 100% owner of the Joint Venture at the time the Poplar Put Right became effective. The Company has determined that it holds a variable interest in the Joint Venture and is the primary beneficiary of the variable interest entity (“VIE”). See Note 2 - Summary of Significant Accounting Policies for further discussion regarding consolidation of variable interest entities.

The business purpose of the Joint Venture is to facilitate and capitalize on the combined capabilities, resources and healthcare industry relationships of its members by partnering, promoting and providing oncology services to office based physicians, hospitals and medical centers. Operational services of the Joint Venture are performed entirely by its members and employees of its members. Precipio SPV’s responsibilities include product and account management services, selling & marketing, laboratory diagnostic services and general & administrative services. Precipio SPV is entitled to a management fee for the services it provides. This management fee is established through service agreements

which were executed in conjunction with the formation of the Joint Venture. Poplar receives a similar fee for the billing services that it provides.

*Going Concern.*

The condensed consolidated financial statements have been prepared using accounting principles generally accepted in the United States of America (“GAAP”) applicable for a going concern, which assume that the Company will realize its assets and discharge its liabilities in the ordinary course of business. The Company has incurred substantial operating losses and has used cash in its operating activities for the past several years. As of September 30, 2020, the Company had a net loss of \$8.7 million, negative working capital of \$0.5 million and net cash used in operating activities of \$6.0 million. The Company’s ability to continue as a going concern over the next twelve months from the date of issuance of these condensed consolidated financial statements in this Quarterly Report on Form 10-Q is dependent upon a combination of achieving its business plan, including generating additional revenue and avoiding potential business disruption due to the novel coronavirus (“COVID-19”) pandemic, and raising additional financing to meet its debt obligations and paying liabilities arising from normal business operations when they come due.

To meet its current and future obligations the Company has taken the following steps to capitalize the business and successfully achieve its business plan:

- On March 26, 2020, the Company entered into a second purchase agreement (the “LP 2020 Purchase Agreement”) with Lincoln Park Capital Fund LLC (“Lincoln Park”), pursuant to which Lincoln Park has agreed to purchase from the Company up to an aggregate of \$10.0 million of common stock of the Company (subject to certain limitations) from time to time over the term of the LP 2020 Purchase Agreement. The extent we rely on Lincoln Park as a source of funding will depend on a number of factors including, the prevailing market price of our common stock and the extent to which we are able to secure working capital from other sources. As of the date of issuance of this Quarterly Report on Form 10-Q, we have already received \$6.7 million from the LP 2020 Purchase Agreement from the sale of 4,130,000 shares of common stock to Lincoln Park from April 1, 2020 through the date of issuance of this Form 10-Q, leaving the Company an additional \$3.3 million to draw subsequent to the filing of this Quarterly Report. See Note 8 Stockholders’ Equity for further discussion on Lincoln Park agreements; and
- The Company filed with the SEC a registration statement on Form S-3 on March 27, 2020, as amended on April 9, 2020, to register an indeterminate number of shares of common stock and preferred stock, such indeterminate principal amount of debt securities and such indeterminate number of warrants to purchase common stock, preferred stock or debt securities as shall have an aggregate initial offering price not to exceed \$50 million. This registration statement was declared effective by the SEC on April 13, 2020 and allows the Company, from time to time, to offer up to \$50 million of any combination of the securities described in the Form S-3 in one or more offerings. In order for the Company to utilize the effective S-3, it will have to file subsequent prospectus supplement(s) with regard to the securities it will offer, as applicable from time to time. As of the date of issuance of this Form 10-Q, no subsequent prospectus supplements to this effect have been filed by the Company.

Notwithstanding the aforementioned circumstances, there remains substantial doubt about the Company’s ability to continue as a going concern for the next twelve months from the date these condensed consolidated financial statements were issued. There can be no assurance that the Company will be able to successfully achieve its initiatives summarized above in order to continue as a going concern over the next twelve months from the date of issuance of this Quarterly Report Form 10-Q. The accompanying condensed consolidated financial statements have been prepared assuming the Company will continue as a going concern and do not include any adjustments that might result should the Company be unable to continue as a going concern as a result of the outcome of this uncertainty.

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## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### *Basis of Presentation.*

The accompanying condensed consolidated financial statements are presented in conformity with GAAP and, as of September 30, 2020 and for the nine months ended September 30, 2020 and 2019, are unaudited and reflect all adjustments (consisting of only normal recurring adjustments) that are necessary for a fair presentation of the financial position and operating results for the interim periods. These unaudited condensed consolidated financial statements and notes should be read in conjunction with the audited financial statements and notes thereto for the year ended December 31, 2019 contained in our Annual Report on Form 10-K, filed with the Securities and Exchange Commission (the “SEC”) on March 27, 2020, and as amended on April 7, 2020. The results of operations for the interim periods presented are not necessarily indicative of the results for fiscal year 2020.

The condensed consolidated financial statements include the accounts of Precipio and its wholly owned subsidiaries, and the Joint Venture which is a VIE in which we are the primary beneficiary. Refer to the section titled “Consolidation of Variable Interest Entities” for further information related to our accounting for the Joint Venture. All intercompany balances have been eliminated in consolidation.

### *Recently Adopted Accounting Pronouncements.*

In August 2018, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2018-13 “*Fair Value Measurement (Topic 820)*”, which modifies certain disclosure requirements in Topic 820, such as the removal of the need to disclose the amount of and reason for transfers between Level 1 and Level 2 of the fair value hierarchy, and several changes related to Level 3 fair value measurements. The Company adopted this guidance on January 1, 2020. The adoption of this guidance was not material to our condensed consolidated financial statements.

In August 2018, the FASB issued ASU 2018-15 “*Intangibles—Goodwill and Other—Internal Use Software (Subtopic 350-40)*”, which aligns the requirements for capitalizing implementation costs incurred in a cloud computing hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal use software. The Company adopted this guidance on January 1, 2020. The adoption of this guidance was not material to our condensed consolidated financial statements.

### *Recent Accounting Pronouncements Not Yet Adopted.*

In August 2020, the FASB issued ASU 2020-06 “*Debt—Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging—Contracts in Entity’s Own Equity (Subtopic 815-40): Accounting for Convertible Instruments and Contracts in an Entity’s Own Equity.*” This ASU amends the guidance on convertible instruments and the derivatives scope exception for contracts in an entity’s own equity and improves and amends the related EPS guidance for both Subtopics. The ASU will be effective for annual reporting periods after December 15, 2023 and interim periods within those annual periods and early adoption is permitted in annual reporting periods ending after December 15, 2020. The Company is currently assessing the potential impact that the adoption of this ASU will have on its condensed consolidated financial statements.

In December 2019, the FASB issued ASU 2019-12 “*Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes*”, which is intended to improve consistent application and simplify the accounting for income taxes. This ASU removes certain exceptions to the general principles in Topic 740 and clarifies and amends existing guidance. This standard is effective for annual reporting periods beginning after December 15, 2020, including interim

reporting periods within those annual reporting periods, with early adoption permitted. The Company is currently evaluating the impact of adoption of this ASU and does not expect the adoption of this new standard to have a material impact on its condensed consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13 “*Measurement of Credit Losses on Financial Instruments*”, which replaces current methods for evaluating impairment of financial instruments not measured at fair value, including trade accounts receivable and certain debt securities, with a current expected credit loss model. This ASU, as amended, is

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effective for the Company for reporting periods beginning after December 15, 2022. The Company is currently assessing the potential impact that the adoption of this ASU will have on its condensed consolidated financial statements.

*Loss Per Share.*

Basic loss per share is calculated based on the weighted-average number of common shares outstanding during each period. Diluted loss per share includes shares issuable upon exercise of outstanding stock options, warrants or conversion rights that have exercise or conversion prices below the market value of our common stock. Options, warrants and conversion rights pertaining to 1,832,514 and 1,725,719 shares of our common stock have been excluded from the computation of diluted loss per share at September 30, 2020 and 2019, respectively, because the effect is anti-dilutive due to the net loss.

The following table summarizes the outstanding securities not included in the computation of diluted net loss per share:

	September 30,	
	2020	2019
Stock options	808,245	493,908
Warrants	906,769	909,189
Preferred stock	117,500	20,888
Convertible notes	—	301,734
Total	<u>1,832,514</u>	<u>1,725,719</u>

*Consolidation of Variable Interest Entities.*

We evaluate any entity in which we are involved to determine if the entity is a VIE and if so, whether we hold a variable interest and are the primary beneficiary. We consolidate VIEs that are subject to assessment when we are deemed to be the primary beneficiary of the VIE. The process for determining whether we are the primary beneficiary of the VIE is to conclude whether we are a party to the VIE holding a variable interest that meets both of the following criteria: (1) has the power to make decisions that most significantly affect the economic performance of the VIE, and (2) has the obligation to absorb losses or the right to receive benefits that in either case could potentially be significant to the VIE.

We have determined that we hold a variable interest in the Joint Venture, have the power to make significant operational decisions on behalf of the VIE and also have the obligation to absorb the majority of the losses from the VIE. As such we have also determined that we are the primary beneficiary of the VIE. The following table presents information about the carrying value of the assets and liabilities of the Joint Venture which we consolidate and which are included on our condensed consolidated balance sheets. Intercompany balances are eliminated in consolidation and not reflected in the following table.

(dollars in thousands)	September 30, 2020
<b>Assets:</b>	
Accounts receivable, net	\$ 569
Total assets	<u>\$ 569</u>
<b>Liabilities:</b>	
Accrued expenses	\$ 7
Total liabilities	<u>\$ 7</u>
<b>Noncontrolling interest in Joint Venture</b>	<u>\$ 27</u>

The Company entered into the Joint Venture during 2020 and, as such, there are no assets or liabilities of the Joint Venture as of December 31, 2019.

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### 3. LONG-TERM DEBT

Long-term debt consists of the following:

	<b>Dollars in Thousands</b>	
	<b>September 30, 2020</b>	<b>December 31, 2019</b>
Department of Economic and Community Development (DECD)	\$ 240	\$ 249
DECD debt issuance costs	(22)	(24)
Financed insurance loan	19	260
September 2018 Settlement	6	34
Paycheck Protection Program	787	—
Total long-term debt	1,030	519
Current portion of long-term debt	(530)	(321)
Long-term debt, net of current maturities	<u>\$ 500</u>	<u>\$ 198</u>

*Department of Economic and Community Development.*

On January 8, 2018, the Company received gross proceeds of \$400,000 when it entered into an agreement with the Department of Economic and Community Development (“DECD”) by which the Company received a grant of \$100,000 and a loan of \$300,000 secured by substantially all of the Company’s assets (the “DECD 2018 Loan”). The DECD 2018 Loan is a ten-year loan due on December 31, 2027 and includes interest paid monthly at 3.25%.

Due to the economic impact of COVID-19, DECD offered financial relief to all businesses with certain loans, including the Company’s DECD 2018 Loan. The relief includes the option to defer all payments from April 1, 2020 to August 1, 2020 and the deferred payments will be added to the end of the loan. The Company chose to defer its payments and the maturity date of the DECD 2018 Loan was extended to May 31, 2028. The payment deferral modification did not have a material impact on the Company’s cash flows for the nine months ended September 30, 2020.

Debt issuance costs associated with the DECD 2018 Loan were approximately \$31,000. Amortization of the debt issuance costs were less than \$1,000 for the three months ended September 30, 2020 and 2019, respectively, and \$2,000 for the nine months ended September 30, 2020 and 2019, respectively. Net debt issuance costs were approximately \$22,000 and \$24,000 at September 30, 2020 and December 31, 2019, respectively, and are presented as a reduction of the related debt in the accompanying condensed consolidated balance sheets. Amortization for each of the next five years is expected to be approximately \$3,000.

*Financed Insurance Loan.*

The Company finances certain of its insurance premiums (the “Financed Insurance Loans”). In July 2018, the Company financed \$0.4 million with a 4.89% interest rate and fully paid off such loan as of July 2019. In July 2019, the Company financed \$0.4 million with a 5.0% interest rate and made monthly payments through May of 2020. In July 2020, the Company financed less than \$0.1 million with a 5.0% interest rate and will make monthly payments through May 2021. As of September 30, 2020 and December 31, 2019, the Financed Insurance Loan’s outstanding balance of less than \$0.1 million and \$0.3 million, respectively, was included in current maturities of long-term debt in the Company’s condensed consolidated balance sheet. A corresponding prepaid asset was included in other current assets.

*Settlement Agreement.*

On September 21, 2018, the Company entered into a settlement and forbearance agreement with a creditor (the “September 2018 Settlement”) pursuant to which, the Company agreed to make monthly principal and interest payments to the creditor over a two year period, from November 1, 2018 to November 1, 2020, in full and final settlement of \$0.1 million of indebtedness that was owed to the creditor on the date of the September 2018 Settlement. The settlement amount accrues interest at the rate of 10% per annum until paid in full. The September 2018 Settlement outstanding balance of



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less than \$0.1 million was included in current maturities of long-term debt in the Company's condensed consolidated balance sheet as of September 30, 2020 and December 31, 2019, respectively.

*Paycheck Protection Program.*

On April 23, 2020, the Company entered into a promissory note (the "Promissory Note") evidencing an unsecured \$787,200 loan under the Paycheck Protection Program (the "PPP Loan"). The Paycheck Protection Program (or "PPP") was established under the recently congressionally-approved Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act") and is administered by the U.S. Small Business Administration. The PPP Loan to the Company was made through Webster Bank, N.A.

The term of the PPP Loan is two years. The interest rate on the PPP Loan is 1.00% and payments are deferred for the first six months of the term of the loan. Under the terms of the CARES Act, PPP Loan recipients can apply for and be granted forgiveness for all or a portion of loans granted under the PPP. Such forgiveness will be determined, subject to limitations, based on the use of loan proceeds for payroll costs and mortgage interest, rent or utility costs and the maintenance of employee and compensation levels. The Company will use the eight-week forgiveness period and will apply for forgiveness of the PPP Loan in accordance with the terms of the PPP, but no assurance is provided that the Company will obtain forgiveness of the PPP Loan in whole or in part. The Company believes it used all of the PPP Loan amount for qualifying expenses. As of the date of issuance of this Report on Form 10-Q, using the eight-week forgiveness period, the Company has incurred approximately \$0.8 million in payroll, payroll related costs and other anticipated qualifying expenses.

The Promissory Note contains customary events of default relating to, among other things, payment defaults, breach of representations and warranties, or provisions of the Promissory Note. The occurrence of an event of default may result in the repayment of all amounts outstanding, collection of all amounts owing from the Company, and/or filing suit and obtaining judgment against the Company.

As of September 30, 2020, \$0.5 million the PPP Loan's outstanding balance was included in current maturities of long-term debt and \$0.3 million was included in long-term debt in the Company's condensed consolidated balance sheet.

#### 4. CONVERTIBLE NOTES

Convertible notes consist of the following:

	<u>Dollars in Thousands</u>	
	<u>September 30, 2020</u>	<u>December 31, 2019</u>
Convertible bridge notes	\$ —	\$ 1,938
Convertible bridge notes discount and debt issuance costs	—	(1,796)
Total convertible notes	—	142
Current portion of convertible notes	—	(142)
Convertible notes, net of current maturities	<u>\$ —</u>	<u>\$ —</u>

*Convertible Bridge Notes.*

On April 20, 2018, the Company entered into a securities purchase agreement (the “2018 Note Agreement”) with certain investors (the “April 2018 Investors”), as amended on November 29, 2018 (the “Amendment Agreement”) and amended on April 16, 2019 (“Amendment No.2 Agreement”). During 2018, pursuant to the 2018 Note Agreement, the Company issued approximately \$4.5 million in Senior Secured Convertible Promissory Notes (the “Bridge Notes”) along with warrants.

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On April 16, 2019, the Company entered into the Amendment No.2 Agreement which provided the Company with approximately \$900,000 of gross proceeds for the issuance of notes with an aggregate principal of \$989,011 (the “April 2019 Bridge Notes”) together with applicable warrants, with substantially the same terms and conditions as the previously issued Bridge Notes and related warrants. The 9% discount associated with the April 2019 Bridge Notes was approximately \$89,000 and was recorded as a debt discount. In connection with the April 2019 Bridge Note issuances, the Company issued to the investors 147,472 warrants to purchase shares of common stock of the Company with a five year term and exercise price of \$5.40 (the “April 2019 Warrants”). The April 2019 Warrants had an initial value of approximately \$1.0 million at the date of issuance and were recorded as a liability with an offset to debt discount. See Note 9 – Fair Value for further discussion. The April 2019 Bridge Notes were issued to investors that previously participated in the 2018 Note Agreement.

The conversion price of the April 2019 Bridge Notes shall be equal to the greater of \$3.75 or \$0.75 above the closing bid price of our common stock on the date prior to the original issue date. In the event the notes are not paid in full prior to 180 days after the original issue date, the conversion price shall be equal to 80% of the lowest volume weighted average price (“VWAP”) in the 10 trading days prior to the date of the notice of conversion, but in no event below the floor price of \$2.25.

The Company reviewed the conversion option of the April 2019 Bridge Notes and determined that there was a beneficial conversion feature with a value of approximately \$0.9 million which was recorded as a debt discount with an offset to additional paid in capital at the time of the Amendment No.2 Agreement. The Company also reviewed the redemption features of the April 2019 Bridge Notes and determined that there is a redemption feature (the “Bridge Notes Redemption Feature”) that qualifies as an embedded derivative. The Company performed a valuation at the time of issuance which resulted in zero value, at that time, due to the high value of the conversion feature and a limited upside from the redemption premium.

Debt discounts and debt issuance costs related to the April 2019 Bridge Notes totaled \$2.0 million. Since the costs exceeded the \$1.0 million face amount of the debt at issuance, the Company recorded \$1.0 million of debt discount and debt issuance costs as a reduction of the related debt in the accompanying consolidated balance sheet with the excess \$1.0 million expensed as a loss on issuance of convertible notes in the consolidated statements of operations during the nine months ended September 30, 2019.

Pursuant to the Amendment No.2 Agreement, previously issued warrants were amended such that the exercise price of such warrants was amended from \$7.50 to \$5.40 and any warrant that had a one-year term was amended to have a five-year term. The Company reviewed the amendments to the warrants and determined that they will be treated as a modification of an outstanding equity instrument at the time of the Amendment No.2 Agreement. Management calculated the change in fair value due to the modifications to be an expense of approximately \$1.1 million which is included in loss on modification of warrants in the condensed consolidated statements of operations during the nine months ended September 30, 2019.

On May 14, 2019, the Company entered into a securities purchase agreement pursuant to which, the Company was provided with \$1,000,000 of gross proceeds for the issuance of notes with an aggregate principal of \$1,098,901 (the “May 2019 Bridge Notes”) together with applicable warrants, with substantially the same terms and conditions as the previously issued Bridge Notes and related warrants. The 9% discount associated with the May 2019 Bridge Notes was approximately \$99,000 and was recorded as a debt discount. In connection with the May 2019 Bridge Note issuances, the Company issued to the investors 154,343 warrants to purchase shares of common stock of the Company with a five year term and exercise price of \$9.56 (the “May 2019 Warrants”). The May 2019 Warrants had an initial value of approximately \$0.9 million at the date of issuance and were recorded as a liability with an offset to debt discount. See Note 9 – Fair Value for further discussion. The May 2019 Bridge Notes were issued to investors that previously participated in the 2018 Note Agreement.

The conversion price of the May 2019 Bridge Notes is \$7.12, provided that a) in the event the notes are not paid in full prior to 180 days after the original issue date or b) upon a registration statement (as defined in the purchase agreement) being declared effective, whichever occurs earlier, the conversion price shall be equal to 80% of the lowest VWAP in the 10 trading days prior to the date of the notice of conversion, but in no event below the floor price of \$2.25.

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The Company reviewed the conversion option of the May 2019 Bridge Notes and determined that there was a beneficial conversion feature with a value of approximately \$0.9 million which was recorded as a debt discount with an offset to additional paid in capital at the time of issuance of the May 2019 Bridge Notes. The May 2019 Bridge Notes also contain the Bridge Notes Redemption Feature and the Company performed a valuation at the time of issuance which resulted in zero value, at that time, due to the high value of the conversion feature and a limited upside from the redemption premium.

Debt discounts and debt issuance costs related to the May 2019 Bridge Notes totaled \$2.0 million. Since the costs exceeded the \$1.1 million face amount of the debt, the Company recorded \$1.1 million of debt discount and debt issuance costs as a reduction of the related debt in the accompanying consolidated balance sheet with the excess \$0.9 million expensed as a loss on issuance of convertible notes in the consolidated statements of operations during the nine months ended September 30, 2019.

On March 26, 2020, the Company entered into an amendment agreement (the “March 2020 Amendment”) amending the terms of that certain Amendment No. 2 Agreement dated April 16, 2019 and the securities purchase agreement dated May 14, 2019. As a result of the March 2020 Amendment, (i) the maturity date of the April 2019 Bridge Notes and the May 2019 Bridge Notes was extended three months from April 16, 2020 to July 16, 2020, (ii) the floor price at which conversions may occur under the April 2019 Bridge Notes and the May 2019 Bridge Notes was amended from \$2.25 to \$0.40, and (iii) guaranteed interest on the April 2019 Bridge Notes and the May 2019 Bridge Notes was amended from twelve months to eighteen months.

The Company reviewed the modifications and concluded that the March 2020 Amendment will be treated as an extinguishment of the related April 2019 Bridge Notes and May 2019 Bridge Notes. The difference between the carrying value of the notes just prior to modification (the “Pre-modification Debt”) and the fair value of the notes just after modification (the “Post-modification Debt”) would be recorded as a gain or loss on extinguishment in the

condensed consolidated statements of operations. The Company removed the carrying value of the Pre-modification Debt which included \$1.0 million of unamortized debt discounts and beneficial conversion features of \$0.5 million. The Company calculated the fair value of the Post-modification Debt to be \$2.6 million. The Company reviewed whether or not a beneficial conversion feature existed on the Post-modification Debt but the calculation resulted in zero intrinsic value so no new beneficial conversion feature was recorded. Management also reviewed the Bridge Notes Redemption Feature of the post-modification notes but their fair value was zero so no derivative liability was recorded at the time of modification, however this will be reassessed at the end of each reporting period. As a result, the Company recorded a debt premium on the Post-modification Debt of \$0.8 million and a loss on extinguishment of convertible notes of \$1.2 million in the condensed consolidated statements of operations during the nine months ended September 30, 2020.

During the three months ended September 30, 2020, there were no bridge note conversions. During the three months ended September 30, 2019, \$0.1 million of bridge notes, plus interest, were converted into 52,748 shares of common stock of the Company. During the nine months ended September 30, 2020 and 2019, \$2.2 million and \$4.6 million, respectively, of bridge notes, plus interest, were converted into 3,908,145 and 1,828,766 shares of common stock of the Company, respectively.

As a result of the bridge note conversions, the Company wrote off approximately \$0.5 million of derivative liability, with an offset to additional paid-in capital, during the nine months ended September 30, 2019.

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During the three and nine months ended September 30, 2020 and 2019, the change in Bridge Note debt discounts and debt premiums was as follows:

(Dollars in thousands)

	<b>For the Three Months Ended September 30,</b>			
	<b>2020</b>		<b>2019</b>	
	<b>Debt Discounts</b>	<b>Debt Premiums</b>	<b>Debt Discounts</b>	<b>Debt Premiums</b>
Beginning balance at July 1	\$ —	\$ —	\$ (2,158)	\$ —
Deductions:				
Amortization (1)	—	—	41	—
Write-off related to note conversions (2)	—	—	63	—
Balance at September 30	<u>\$ —</u>	<u>\$ —</u>	<u>\$ (2,054)</u>	<u>\$ —</u>

	<b>For the Nine Months Ended September 30,</b>			
	<b>2020</b>		<b>2019</b>	
	<b>Debt Discounts</b>	<b>Debt Premiums</b>	<b>Debt Discounts</b>	<b>Debt Premiums</b>
Beginning balance at January 1	\$ (1,796)	\$ —	\$ (1,111)	\$ 647
Additions:	—	793	(2,086)	—

Deductions:				
Amortization (accretion) (1)	703	(385)	154	(167)
Write-off related to note conversions (2)	138	(408)	989	(480)
Write-off related to note extinguishment (3)	955	—	—	—
Balance at September 30	<u>\$ —</u>	<u>\$ —</u>	<u>\$ (2,054)</u>	<u>\$ —</u>

- (1) Amortization/accretion is recognized as interest expense/income within the condensed consolidated statements of operations based on the effective interest method.
- (2) Write-offs associated with note conversions are recognized as an offset to additional paid-in capital at the time of the conversion.
- (3) Write-offs associated with note extinguishment are recognized as a loss and included in loss on extinguishment of convertible notes in the condensed consolidated statements of operations.

*Convertible Promissory Notes – Exchange Notes.*

During the three and nine months ended September 30, 2019, zero and \$0.6 million, respectively, of previously issued convertible promissory notes (the “Exchange Notes”) were converted into zero and 155,351 shares of common stock of the Company, respectively.

As of September 30, 2020 and December 31, 2019, the outstanding balance of the Exchange Notes, net of discounts, was zero, respectively.

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There was no Exchange Note activity during the three months ended September 30, 2019. During the nine months ended September 30, 2019, the change in Exchange Note debt discounts was as follows:

(Dollars in thousands)

	<b>For the Nine Months Ended September 30, 2019</b>
Beginning balance at January 1	\$ (83)
Deductions:	
Amortization (1)	2
Write-off related to note conversions (2)	81
Balance at September 30	<u>\$ —</u>

- (1) Amortization is recognized as interest expense within the condensed consolidated statements of operations based on the effective interest method.
- (2) Write-offs associated with note conversions are recognized as an offset to additional paid-in capital at the time of the conversion.

As a result of Exchange Note conversions, during the three and nine months ended September 30, 2019, the Company wrote off zero and less than \$0.1 million, respectively, of derivative liability with an offset to additional paid-in capital.

*Convertible Promissory Notes – Crede Note.*

On January 15, 2019, the Company and Crede Capital Group LLC (“Crede”) entered into an amendment and restatement agreement (the “Crede Amendment Agreement”) in order to enable the Company to provide Crede with an alternative means of payment of a previous settlement amount, by issuing to Crede a convertible note in the amount of \$1.45 million (the “Crede Note”). The conversion price of the Crede Note shall equal 90% of the closing bid price of the Company’s common stock on the date prior to each conversion date. The Crede Note is payable by the Company on the earlier of (i) January 15, 2021 or (ii) upon the closing of a qualified offering in which the Company receives gross proceeds of at least \$4.0 million. The Crede Note may not be converted if, after giving effect to the conversion, Crede together with its affiliates would beneficially own in excess of 4.99% of the outstanding shares of the Company’s common stock. The Company, at its option, may redeem some or all of the then outstanding principal amount of the Crede Note for cash.

In accordance with the terms of the Crede Amendment Agreement, during the period commencing on the date of issuance of the Crede Note and ending on the date Crede no longer beneficially owns any portion of the Crede Note, Crede shall not sell, on any given trading day, more than the greater of (i) \$10,000 of common stock (subject to adjustment for any stock splits or combinations, stock dividends, recapitalizations or similar event after the date hereof) and (ii) 10% of the daily average composite trading volume of the Company’s common stock as reported by Bloomberg, LP (subject to adjustment for any stock splits or combinations, stock dividends, recapitalizations or similar event after the date hereof) for such trading day.

During the three and nine months ended September 30, 2019, the Company made no payments on the Crede Note. On April 16, 2019, the entire outstanding amount of \$1.45 million was converted into 270,699 shares of common stock of the Company and as of September 30, 2020 and December 31, 2019; the remaining amount due on the Crede note was zero.

*Convertible Promissory Notes – Leviston Note*

On February 8, 2018, the Company entered into an equity purchase agreement (the “2018 Purchase Agreement”) with Leviston Resources LLC (“Leviston”). On January 29, 2019, the Company entered into a settlement agreement (the “Leviston Settlement”) with Leviston pursuant to which the Company issued to Leviston a convertible note in the amount of \$0.7 million (the “Leviston Note”) in full satisfaction of certain obligations to Leviston.

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In addition to the Leviston Settlement and the Leviston Note, the Company and Leviston have each executed a release pursuant to which each of the Company and Leviston agreed to release the other party from their respective obligations arising from or concerning the Obligations.

During the three and nine months ended September 30, 2019, the Company made cash payments of zero and less than \$0.1 million, respectively, on the Leviston Note. During the three and nine months ended September 30,

2019, zero and \$0.7 million, respectively, of the Leviston Note was converted into zero and 184,357 shares of common stock of the Company, respectively.

The remaining amount due on the Leviston Note was zero as of September 30, 2020 and December 31, 2019, respectively.

## 5. ACCRUED EXPENSES OTHER CURRENT LIABILITIES.

Accrued expenses at September 30, 2020 and December 31, 2019 are as follows:

(dollars in thousands)	September 30, 2020	December 31, 2019
Accrued expenses	\$ 1,247	\$ 1,268
Accrued compensation	536	247
Accrued interest	21	124
	<u>\$ 1,804</u>	<u>\$ 1,639</u>

During the three and nine months ended September 30, 2019, the Company recorded gain on settlement of liability, net of zero and \$1.3 million, respectively, from the settlement of obligations with certain vendors. There were no gains on settlement of liability recorded during the three and nine months ended September 30, 2020.

## 6. COMMITMENTS AND CONTINGENCIES

The Company is involved in legal proceedings related to matters, which are incidental to its business. Also, the Company is delinquent on the payment of outstanding accounts payable for certain vendors and suppliers who have taken or have threatened to take legal action to collect such outstanding amounts. See below for a discussion on these matters.

### LITIGATIONS

CPA Global provides us with certain patent management services. On February 6, 2017, CPA Global claimed that we owed approximately \$0.2 million for certain patent maintenance services rendered. CPA Global has not filed claims against us in connection with this allegation. A liability of less than \$0.1 million has been recorded and is reflected in accounts payable within the accompanying condensed consolidated balance sheets at September 30, 2020 and December 31, 2019.

On February 17, 2017, Jesse Campbell (“Campbell”) filed a lawsuit individually and on behalf of others similarly situated against us in the District Court for the District of Nebraska alleging we had a materially incomplete and misleading proxy relating to a potential merger and that the merger agreement’s deal protection provisions deter superior offers. On June 21, 2019, the parties filed a stipulation of settlement, in which defendants are released from all claims and expressly deny that they have committed any act or omission giving rise to any liability. The stipulation includes a settlement payment of \$1.95 million. On July 10, 2019, the Court entered an order preliminarily approving the settlement. During the third quarter of 2019, both the Company and its insurance company paid their respective amounts of \$0.27 million and \$1.68 million, respectively, to an escrow account where the funds were held until they were approved for distribution. On June 3, 2020, the Court approved the settlement and entered an order of dismissal. As of the date the condensed consolidated financial statements were issued, the escrow funds have been released and this matter is closed.

## *LEGAL AND REGULATORY ENVIRONMENT*

The healthcare industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not limited to, matters such as licensure, accreditation, government healthcare program participation requirement, reimbursement for patient services and Medicare and Medicaid fraud and abuse. Government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers.

Violations of these laws and regulations could result in expulsion from government healthcare programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the Company is in compliance with fraud and abuse regulations, as well as other applicable government laws and regulations. While no material regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or unasserted at this time.

## **7. LEASES**

On January 1, 2019, the Company recorded initial ROU assets and corresponding operating lease liabilities of approximately \$750,000 and a reversal of deferred rent and prepaid expenses of approximately \$6,000 resulting in no cumulative effect adjustment upon adoption of Topic 842. The Company leases administrative facilities and laboratory equipment through operating lease agreements. In addition we rent various equipment used in our diagnostic lab and in our administrative offices through finance lease arrangements. Our operating leases include both lease (e.g., fixed payments including rent) and non-lease components (e.g., common area or other maintenance costs). The facility leases include one or more options to renew, from 1 to 5 years or more. The exercise of lease renewal options is typically at our sole discretion, therefore, the renewals to extend the lease terms are not included in our ROU assets and lease liabilities as they are not reasonably certain of exercise. We regularly evaluate the renewal options and, when they are reasonably certain of exercise, we include the renewal period in our lease term. As our leases do not provide an implicit rate, we use our collateralized incremental borrowing rate based on the information available at the lease commencement date in determining the present value of the lease payments.

Operating leases result in the recognition of ROU assets and lease liabilities on the balance sheet. ROU assets represent our right to use the leased asset for the lease term and lease liabilities represent our obligation to make lease payments. Operating lease ROU assets and liabilities are recognized at commencement date based on the present value of lease payments over the lease term. Lease expense is recognized on a straight-line basis over the lease term. Leases with an initial term of 12 months or less are not recorded on the balance sheet. The primary leases we enter into with initial terms of 12 months or less are for equipment.

Upon the adoption of Topic 842, our accounting for finance leases, previously referred to as capital leases, remains substantially unchanged from prior guidance.



The balance sheet presentation of our operating and finance leases is as follows:

(dollars in thousands)

	<u>Classification on the Condensed Consolidated Balance Sheet</u>	<u>September 30, 2020</u>	<u>December 31, 2019</u>
<b>Assets:</b>			
Operating lease assets	Operating lease right-of-use assets, net	\$ 358	\$ 519
Finance lease assets	Property and equipment, net	187	184
<b>Total lease assets</b>		<u>\$ 545</u>	<u>\$ 703</u>
<b>Liabilities:</b>			
Current:			
Operating lease obligations	Current maturities of operating lease liabilities	\$ 219	\$ 209
Finance lease obligations	Current maturities of finance lease liabilities	37	52
Noncurrent:			
Operating lease obligations	Operating lease liabilities, less current maturities	150	317
Finance lease obligations	Finance lease liabilities, less current maturities	108	119
<b>Total lease liabilities</b>		<u>\$ 514</u>	<u>\$ 697</u>

As of September 30, 2020 and December 31, 2019, the estimated future minimum lease payments, excluding non-lease components, are as follows:

(dollars in thousands)

	<u>Operating Leases</u>		<u>Finance Leases</u>	
	<u>September 30, 2020</u>	<u>December 31, 2019</u>	<u>September 30, 2020</u>	<u>December 31, 2019</u>
2020	\$ 59	\$ 242	\$ 13	\$ 62
2021	241	241	50	38
2022	48	48	38	32
2023	35	35	28	28
2024	17	17	27	27
Thereafter	—	—	13	13
Total lease obligations	400	583	169	200
Less: Amount representing interest	(31)	(57)	(24)	(29)
Present value of net minimum lease obligations	369	526	145	171
Less, current portion	(219)	(209)	(37)	(52)
Long term portion	<u>\$ 150</u>	<u>\$ 317</u>	<u>\$ 108</u>	<u>\$ 119</u>

Other information as of September 30, 2020 and December 31, 2019:

	<u>September 30, 2020</u>	<u>December 31, 2019</u>
Weighted-average remaining lease term (years):		
Operating leases	2.0	2.8
Finance leases	4.0	4.3
Weighted-average discount rate:		
Operating leases	8.00%	8.00%
Finance leases	8.19%	7.25%

During the nine months ended September 30, 2020 and 2019, operating cash flows from operating leases was \$0.2 million, respectively, and ROU assets obtained in exchange for operating lease liabilities was zero and \$0.8 million, respectively.

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*Operating Lease Costs*

Operating lease costs were approximately \$0.1 million and \$0.2 million during the three and nine months ended September 30, 2020 and 2019, respectively. These costs are primarily related to long-term operating leases for the Company's facilities and laboratory equipment. Short-term and variable lease costs were less than \$0.1 million for the three and nine months ended September 30, 2020 and 2019, respectively. Cash paid for amounts included in the measurement of operating lease liabilities was approximately \$0.2 million in operating cash flows for the nine months ended September 30, 2020 and 2019, respectively.

*Finance Lease Costs*

Finance leases are included in property and equipment, net and finance lease liabilities, less current maturities on the condensed consolidated balance sheets. The associated amortization expense and interest expense are included in the condensed consolidated statements of operations for the nine months ended September 30, 2020 and 2019. The balances within these accounts are less than \$0.1 million, respectively.

## **8. STOCKHOLDERS' EQUITY**

*Common Stock.*

Pursuant to our Third Amended and Restated Certificate of Incorporation, as amended, we currently have 150,000,000 shares of common stock authorized for issuance. On December 20, 2018, the Company's shareholders approved the proposal to authorize the Company's Board of Directors to, in its discretion, amend the Company's Third Amended and Restated Certificate of Incorporation to increase the total number of authorized shares of common stock from 150,000,000 shares to 250,000,000 shares. The Company has not yet effected this increase.

During the three and nine months ended September 30, 2020, the Company issued zero and 3,908,145 shares of its common stock, respectively, in connection with the conversion of convertible notes, plus interest, totaling zero and \$2.2 million, respectively. During the three and nine months ended September 30, 2019, the Company issued 52,748 and 2,439,173 shares of its common stock, respectively, in connection with the conversion of convertible notes, plus interest, totaling \$0.1 million and \$7.4 million, respectively. See Note 4 – Convertible Notes.

During the three and nine months ended September 30, 2019, the Company issued zero and 310,200 shares of its common stock, respectively, in connection with the exercise of zero and 310,200 warrants, respectively. The warrant exercises resulted in net cash proceeds to the Company of approximately \$1.6 million during the nine months ended September 30, 2019.

LP Purchase Agreement

On September 7, 2018, the Company entered into a purchase agreement (the "LP Purchase Agreement") with Lincoln Park, pursuant to which Lincoln Park has agreed to purchase from the Company up to an aggregate of \$10,000,000 of common stock of the Company (subject to certain limitations) from time to time over the term of the LP Purchase Agreement. Pursuant to the terms of the LP Purchase Agreement, on the agreement date, the Company

issued 40,000 shares of its common stock to Lincoln Park as consideration for its commitment to purchase shares of common stock of the Company under the LP Purchase Agreement (the “LP Commitment Shares”). Also on September 7, 2018, the Company entered into a registration rights agreement with Lincoln Park (the “LP Registration Rights Agreement”), pursuant to which on September 14, 2018, the Company filed with the SEC a registration statement on Form S-1 to register for resale under the Securities Act of 1933, as amended, or the Securities Act, 466,667 shares of common stock, which includes the LP Commitment Shares, that have been or may be issued to Lincoln Park under the LP Purchase Agreement. The Form S-1 was declared effective by the SEC on September 28, 2018. As of January 16, 2019, all shares registered under this S-1 had been sold and/or issued to Lincoln Park. On February 1, 2019, the Company filed with the SEC a registration statement on Form S-1 to register for resale under the Securities Act of 1933, as amended, or the Securities Act, an additional 1,000,000 shares of common stock that have been or may be issued to Lincoln Park under the LP Purchase Agreement.

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The Form S-1 was declared effective by the SEC on February 12, 2019. As of August 5, 2019, all shares registered under this S-1 had been sold and/or issued to Lincoln Park. On August 9, 2019, the Company filed with the SEC a registration statement on Form S-1 to register for resale under the Securities Act of 1933, as amended, or the Securities Act, an additional 1,800,000 shares of common stock that have been or may be issued to Lincoln Park under the LP Purchase Agreement. As of January 9, 2020, all shares registered under this S-1 had been sold and/or issued to Lincoln Park. On January 14, 2020, the Company filed with the SEC a registration statement on Form S-1 to register for resale under the Securities Act of 1933, as amended, or the Securities Act, an additional 920,654 shares of common stock that have been or may be issued to Lincoln Park under the LP Purchase Agreement. As of April 6, 2020, all 920,654 shares registered under this S-1 had been sold and/or issued to Lincoln Park.

Under the LP Purchase Agreement, the Company may, from time to time and at its sole discretion, on any single business day on which the closing price of its common stock is not less than \$1.50 per share (subject to adjustment for any reorganization, recapitalization, non-cash dividend, stock split, reverse stock split or other similar transaction as provided in the LP Purchase Agreement), direct Lincoln Park to purchase shares of its common stock in amounts up to 30,000 shares, which amounts may be increased to up to 36,666 shares depending on the market price of its common stock at the time of sale and subject to a maximum commitment by Lincoln Park of \$1,000,000 per single purchase, which the Company refers to as “regular purchases”, plus other “accelerated amounts” and/or “additional accelerated amounts” under certain circumstances. The Company will control the timing and amount of any sales of its common stock to Lincoln Park. The purchase price of the shares that may be sold to Lincoln Park in regular purchases under the LP Purchase Agreement will be based on the market price of the common stock of the Company preceding the time of sale as computed under the LP Purchase Agreement. The purchase price per share will be equitably adjusted for any reorganization, recapitalization, non-cash dividend, stock split, or other similar transaction occurring during the business days used to compute such price. The Company may at any time in its sole discretion terminate the LP Purchase Agreement without fee, penalty or cost upon one business day notice. There are no restrictions on future financings, rights of first refusal, participation rights, penalties or liquidated damages in the LP Purchase Agreement or LP Registration Rights Agreement, other than a prohibition on the Company entering into certain types of transactions that are defined in the LP Purchase Agreement as “Variable Rate Transactions.” Lincoln Park may not assign or transfer its rights and obligations under the Purchase Agreement.

Under applicable rules of The Nasdaq Capital Market, in no event may the Company issue or sell to Lincoln Park under the LP Purchase Agreement more than 19.99% of the shares of its common stock outstanding immediately prior to the execution of the LP Purchase Agreement (which is 308,590 shares based on 1,543,724 shares outstanding

immediately prior to the execution of the LP Purchase Agreement), which limitation the Company refers to as the Exchange Cap, unless (i) the Company obtains stockholder approval to issue shares of common stock in excess of the Exchange Cap or (ii) the average price of all applicable sales of the Company's common stock to Lincoln Park under the LP Purchase Agreement equals or exceeds \$7.05 (which represents the closing consolidated bid price of the Company's common stock on September 7, 2018, plus an incremental amount to account for the issuance of the LP Commitment Shares to Lincoln Park), such that issuances and sales of the Company's common stock to Lincoln Park under the LP Purchase Agreement would be exempt from the Exchange Cap limitation under applicable Nasdaq rules. In any event, the LP Purchase Agreement specifically provides that the Company may not issue or sell any shares of its common stock under the LP Purchase Agreement if such issuance or sale would breach any applicable Nasdaq rules. The Company received shareholder approval on December 20, 2018.

The LP Purchase Agreement also prohibits the Company from directing Lincoln Park to purchase any shares of common stock if those shares, when aggregated with all other shares of the Company's common stock then beneficially owned by Lincoln Park and its affiliates, would result in Lincoln Park and its affiliates having beneficial ownership, at any single point in time, of more than 4.99% of the then total outstanding shares of the Company's common stock, as calculated pursuant to Section 13(d) of the Securities Exchange Act of 1934, as amended, or the Exchange Act, and Rule 13d-3 thereunder, which limitation the Company refers to as the Beneficial Ownership Cap as defined in the LP Purchase Agreement.

As of the date of issuance of this Quarterly Report on Form 10-Q, we have already received an aggregate of \$9.4 million from the sale of common stock to Lincoln Park under the LP Purchase Agreement, including approximately: \$1.4 million from the sale of 328,590 shares of common stock during 2018; \$6.6 million from the sale of 2,778,077 shares of

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common stock during 2019; and \$1.4 million from the sale of 1,040,654 shares of common stock during the nine months ended September 30, 2020. There were no sales of common stock under the LP Purchase Agreement during the three months ended September 30, 2020. As of April 6, 2020, all registered shares relating to the LP Purchase Agreement had been sold and/or issued to Lincoln Park. The LP Purchase Agreement terminated during our second fiscal quarter of 2020. Effective April 13, 2020, the Company became eligible to sell additional shares to Lincoln Park pursuant to the LP 2020 Purchase Agreement, as discussed below.

LP 2020 Purchase Agreement

On March 26, 2020, the Company entered into a purchase agreement (the "LP 2020 Purchase Agreement") and a registration rights agreement (the "LP 2020 Registration Rights Agreement") with Lincoln Park pursuant to which Lincoln Park has agreed to purchase from us, from time to time, up to \$10,000,000 of our common stock, subject to certain limitations, during the 24 month term of the LP 2020 Purchase Agreement. Pursuant to the terms of the LP 2020 Purchase Agreement, on the agreement date, the Company issued 250,000 shares of its common stock to Lincoln Park as consideration for its commitment to purchase shares of common stock of the Company under the LP Purchase Agreement (the "LP 2020 Commitment Shares"). Pursuant to the terms of the LP 2020 Registration Rights Agreement, on March 27, 2020, as amended on April 8, 2020, the Company filed with the SEC a registration statement on Form S-1 to register for resale under the Securities Act of 1933, as amended, or the Securities Act, 1,770,000 shares of common stock, which includes the LP 2020 Commitment Shares, that have been or may be issued to Lincoln Park under the LP 2020 Purchase Agreement. The Form S-1 was declared effective by the SEC on April 13, 2020. As of

June 22, 2020, all shares registered under this S-1 had been sold and/or issued to Lincoln Park. On June 26, 2020, the Company filed with the SEC a registration statement on Form S-1 to register for resale under the Securities Act of 1933, as amended, or the Securities Act, an additional 4,500,000 shares of common stock that have been or may be issued to Lincoln Park under the LP Purchase Agreement. The Form S-1 was amended twice on July 7, 2020 and declared effective by the SEC on July 7, 2020. For the three and nine months ended September 30, 2020, 2,060,000 shares, respectively, registered under this S-1 had been sold and/or issued to Lincoln Park.

Under the LP 2020 Purchase Agreement, on any business day selected by us, we may direct Lincoln Park to purchase up to 50,000 shares of our common stock on any such business day, which we refer to as a Regular Purchase in the LP 2020 Purchase Agreement, provided, however, that (i) the Regular Purchase may be increased to up to 80,000 shares, provided that the closing sale price is not below \$1.00 on the purchase date and (ii) the Regular Purchase may be increased to up to 100,000 shares, provided that the closing sale price is not below \$1.50 on the purchase date. In each case, the maximum amount of any single Regular Purchase may not exceed \$1,000,000 per purchase. Lincoln Park has no right to require the Company to sell any shares of common stock to Lincoln Park, but Lincoln Park is obligated to make purchases as we direct, subject to certain conditions. The purchase price for Regular Purchases shall be equal to the lesser of: (i) the lowest sale price of the common shares during the purchase date, or (ii) the average of the three (3) lowest closing sale prices of the common shares during the ten (10) business days prior to the purchase date.

Under applicable rules of The Nasdaq Capital Market, in no event may we issue or sell to Lincoln Park under the LP 2020 Purchase Agreement more than 19.99% of the shares of our common stock outstanding immediately prior to the execution of the LP 2020 Purchase Agreement (which is 1,774,024 shares, based on 8,870,129 shares outstanding immediately prior to the execution of the LP 2020 Purchase Agreement), which limitation we refer to as the Exchange Cap, unless (i) we obtain stockholder approval to issue shares of common stock in excess of the Exchange Cap or (ii) the average price of all applicable sales of our common stock to Lincoln Park under the LP 2020 Purchase Agreement equals or exceeds \$0.7306 (which represents the closing consolidated bid price of our common stock on March 25, 2020, plus an incremental amount to account for our issuance of the Commitment Shares to Lincoln Park), such that the transactions contemplated by the LP 2020 Purchase Agreement are exempt from the Exchange Cap limitation under applicable Nasdaq rules. In any event, the LP 2020 Purchase Agreement specifically provides that we may not issue or sell any shares of our common stock under the LP 2020 Purchase Agreement if such issuance or sale would breach any applicable rules or regulations of The Nasdaq Capital Market.

The LP 2020 Purchase Agreement also prohibits us from directing Lincoln Park to purchase any shares of common stock if those shares, when aggregated with all other shares of our common stock then beneficially owned by Lincoln Park and its affiliates, would result in Lincoln Park and its affiliates having beneficial ownership, at any single

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point in time, of more than 4.99% of the then total outstanding shares of our common stock, as calculated pursuant to Section 13(d) of the Securities Exchange Act of 1934, as amended, or the Exchange Act, and Rule 13d-3 thereunder, which limitation we refer to as the Beneficial Ownership Cap.

As of the date of issuance of this Quarterly Report on Form 10-Q, we have already received an aggregate of \$6.7 million from the sale of common stock to Lincoln Park under the LP 2020 Purchase Agreement, including approximately; \$4.3 million and \$5.5 million from the sale of 2,060,000 and 3,580,000 shares of common stock during

the three and nine months ended September 30, 2020, respectively; and \$1.2 million from the sale of 550,000 shares of common stock to Lincoln Park which were sold from October 1, 2020 through the date of issuance of this Quarterly Report on Form 10-Q.

#### *Preferred Stock.*

The Company's Board of Directors is authorized to issue up to 15,000,000 shares of preferred stock in one or more series, from time to time, with such designations, powers, preferences and rights and such qualifications, limitations and restrictions as may be provided in a resolution or resolutions adopted by the Board of Directors.

#### *Series B Preferred Stock.*

The Company filed a Certificate of Designation of Preferences, Rights and Limitations of Series B Convertible Preferred Stock ("Series B Preferred Stock") with the State of Delaware which designates 6,900 shares of our preferred stock as Series B Preferred Stock. The Series B Preferred Stock has a stated value of \$1,000 per share and a par value of \$0.01 per share. The Series B Preferred Stock includes a beneficial ownership blocker but has no dividend rights (except to the extent dividends are also paid on the common stock). On August 28, 2017, the Company completed an underwritten public offering (the "August 2017 Offering") consisting of the Company's Series B Preferred Stock and warrants.

The conversion price of the Series B Preferred Stock contains a down round feature. The Company will recognize the effect of the down round feature when it is triggered. At that time, the effect would be treated as a deemed dividend and as a reduction of income available to common shareholders in our basic earnings per share calculation.

The March 2020 Amendment, see Note 4 – Convertible Notes, triggered the down round feature of the Series B Preferred Stock and, as a result, the conversion price of the Company's Series B Convertible Preferred Stock was automatically adjusted from \$2.25 per share to \$0.40 per share. In connection with the down round adjustment, the Company calculated an incremental beneficial conversion feature of approximately \$3.3 million which was recognized as a deemed dividend at time of the down round adjustment ("Deemed Dividend A").

There were no conversions of Series B Preferred Stock during the three and nine months ended September 30, 2020 and 2019, respectively. At September 30, 2020 and December 31, 2019, the Company had 6,900 shares of Series B designated and issued and 47 shares of Series B outstanding.

#### *Liquidation Preferences*

The following is the liquidation preferences for the Company's preferred stock;

Upon any liquidation, dissolution or winding-up of the Corporation, whether voluntary or involuntary, the holders shall be entitled to receive out of the assets of the Corporation an amount equal to the par value, plus any accrued and unpaid dividends thereon, for each share of Preferred Stock before any distribution or payment shall be made to the holders of the Common Stock, and if the assets of the Corporation shall be insufficient to pay in full such amounts, then the entire assets to be distributed to the holders shall be ratably distributed among the holders in accordance with the respective amounts that would be payable on such shares. If all amounts were paid in full; and thereafter, the holders shall be entitled to receive out of the assets, whether capital or surplus, of the Corporation the same amount that a holder of Common Stock would receive if the Preferred Stock were fully converted to Common Stock which amount shall be paid pari passu with all holders of Common Stock.

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*Common Stock Warrants.*

The following represents a summary of the warrants outstanding as of September 30, 2020:

<i>Warrants</i>	<u>Issue Year</u>	<u>Expiration</u>	<u>Underlying Shares</u>	<u>Exercise Price</u>
(1)	2015	December 2020	272	\$ 747.00
(2)	2016	January 2021	596	\$ 544.50
(3)	2017	June 2022	2,540	\$ 41.25
(3)	2017	June 2022	500	\$ 7.50
(4)	2017	June 2022	6,095	\$ 105.00
(5)	2017	August 2022	25,201	\$ 0.40
(6)	2017	August 2022	4,000	\$ 46.88
(7)	2017	August 2022	47,995	\$ 150.00
(7)	2017	August 2022	9,101	\$ 7.50
(8)	2017	August 2022	16,664	\$ 0.40
(8)	2017	August 2022	7,335	\$ 0.40
(9)	2017	October 2022	666	\$ 0.40
(10)	2018	October 2022	7,207	\$ 112.50
(11)	2018	April 2023	69,964	\$ 5.40
(11)	2018	April 2023	121,552	\$ 5.40
(12)	2018	October 2022	15,466	\$ 11.25
(13)	2018	July 2023	14,671	\$ 5.40
(13)	2018	July 2023	14,672	\$ 5.40
(13)	2018	August 2023	36,334	\$ 5.40
(13)	2018	August 2023	36,334	\$ 5.40
(13)	2018	September 2023	19,816	\$ 5.40
(13)	2018	September 2023	20,903	\$ 5.40
(14)	2018	November 2023	75,788	\$ 5.40
(14)	2018	December 2023	51,282	\$ 5.40
(15)	2019	April 2024	147,472	\$ 5.40
(16)	2019	May 2024	154,343	\$ 9.56
			<u>906,769</u>	

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- (1) These warrants were issued in connection with an offering which was completed in July 2015.
  - (2) These warrants were issued in connection with an offering which was completed in January 2016. Of the remaining outstanding warrants as of September 30, 2020, 357 warrants are recorded as a liability, See Note 9 – Fair Value for further discussion, and 239 are treated as equity.
  - (3) These warrants were issued in connection with a June 2017 merger transaction (the “Merger”).
  - (4) These warrants were issued in connection with the Merger.
  - (5) These warrants were issued in connection with an underwritten public offering completed on August 28, 2017 (the “August 2017 Offering”) and are the August 2017 Offering Warrants discussed below.
  - (6) These warrants were issued in connection with the August 2017 Offering.
  - (7) These warrants were issued in connection with the conversion of our Series A Senior stock, at the time of the closing of the August 2017 Offering.

- (8) These warrants were issued in connection with the conversion of convertible bridge notes, at the time of the closing of the August 2017 Offering, and are the Note Conversion Warrants discussed below.
- (9) These warrants were issued in connection with the waiver of default the Company received in the fourth quarter of 2017 in connection with the Convertible Promissory Notes and are the Convertible Promissory Note Warrants discussed below.
- (10) These warrants were issued in connection with the Debt Obligation settlement agreements and are the Creditor Warrants discussed below.

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- (11) These warrants were issued in connection with the 2018 Note Agreement and are the April 2018 Warrants discussed below.
- (12) These warrants were issued in connection with the 2018 Note Agreement and are the Advisor Warrants discussed below.
- (13) These warrants were issued in connection with the 2018 Note Agreement and are the Q3 2018 Warrants discussed below.
- (14) These warrants were issued in connection with the 2018 Note Agreement and subsequent Amendment Agreement and are the Q4 2018 Warrants discussed below.
- (15) These warrants were issued in connection with the 2018 Note Agreement and subsequent Amendment No. 2 Agreement and are the April 2019 Warrants discussed below.
- (16) These warrants were issued in connection with the May 2019 Bridge Notes and are the May 2019 Warrants discussed below.

During the three and nine months ended September 30, 2020, zero and 2,420 warrants expired, respectively. These warrants had been issued in connection with transactions which were completed in October 2014 and February 2015.

August 2017 Offering Warrants

In connection with the August 2017 Offering, the Company issued 178,666 warrants at an exercise price of \$45.00, which contain a down round provision (the “August 2017 Offering Warrants”). The August 2017 Offering Warrants were exercisable immediately and expire 5 years from date of issuance.

As a result of the March 2020 Amendment, the exercise price of the August 2017 Offering Warrants was adjusted from \$2.25 to \$0.40. At the time the exercise price was adjusted, the Company calculated the fair value of the down round provision on the warrants to be approximately \$6,000 and recorded this as a deemed dividend (“Deemed Dividend B”).

There were zero and 6,800 August 2017 Offering Warrants exercised during the three and nine months ended September 30, 2019, respectively, for proceeds to the Company of zero and \$15,000, respectively. During the three and nine months ended September 30, 2019, the intrinsic value of the August 2017 Offering Warrants exercised was zero and \$36,000, respectively.

Note Conversion Warrants



Upon the closing of the August 2017 Offering, the Company issued 23,999 warrants to purchase the Company's common stock (the "Note Conversion Warrants"). The Note Conversion Warrants have an exercise price of \$45.00 per share and contain a down round provision.

As a result of the March 2020 Amendment, the exercise price of the Note Conversion Warrants was adjusted from \$2.25 to \$0.40. At the time the exercise price was adjusted, the Company calculated the fair value of the down round provision on the warrants to be approximately \$5,000 and recorded this as a deemed dividend ("Deemed Dividend C").

#### Convertible Promissory Note Warrants

The Convertible Promissory Note Warrants had an original exercise price of \$45.00 per share and contain a down round provision.

As a result of the March 2020 Amendment, the exercise price of the Convertible Promissory Note Warrants was adjusted from \$2.25 to \$0.40. At the time the exercise price was adjusted, the Company calculated the fair value of the down round provision on the warrants to be less than \$1,000 and recorded this as a deemed dividend ("Deemed Dividend D").

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### Series C Warrants

In connection with a Series C preferred stock offering during 2017, the Company issued 130,857 warrants at an original exercise price of \$24.45, which contain a down round provision (the "Series C Warrants").

There were zero and 25,037 Series C Warrants exercised during the three and nine months ended September 30, 2019, respectively, for proceeds to the Company of zero and \$56,000, respectively. During the three and nine months ended September 30, 2019, the intrinsic value of the Series C Warrants exercised was zero and \$43,000, respectively.

There were no Series C Warrants outstanding at September 30, 2020 or December 31, 2019.

### Creditor Warrants

In the fourth quarter of 2017, the Company entered into Settlement Agreements with the Creditors pursuant to which the Company agreed to issue, to certain of its Creditors, 7,207 Creditor Warrants to purchase 7,207 shares of the Company's common stock at an exercise price of \$112.50 per share. The Creditor Warrants were issued in February 2018.

### April 2018 Warrants

In connection with the issuance of Bridge Notes in April 2018, the Company issued 243,224 warrants at an exercise price of \$11.25 at time of issuance. At issuance, half of these April 2018 Warrants had a five-year term and half had a one-year term.

In April 2019, as a result of the Amendment No.2 Agreement, the exercise price of the April 2018 Warrants was adjusted to \$5.40 and all April 2018 Warrants that had a one-year term were amended to have a five-year term. Due to these modifications, the change in fair value of the April 2018 Warrants was calculated to be an expense of approximately \$0.7 million which is included in loss on modification of warrants in the consolidated statements of operations for the nine months ended September 30, 2019. The expense for the three months ended September 30, 2019 was zero.

There were zero and 51,708 April 2018 Warrants exercised during the three and nine months ended September 30, 2019, respectively, for proceeds to the Company of zero and \$279,000, respectively. During the nine months ended September 30, 2019, the intrinsic value of the April 2018 Warrants exercised was approximately \$128,000.

#### Advisor Warrants

At the time of the 2018 Note Agreement, the Company issued 15,466 warrants with an exercise price of \$11.25 to a financial advisor.

#### Q3 2018 Warrants

In connection with the issuance of Bridge Notes during the third quarter of 2018, the Company issued 196,340 warrants with an exercise price of \$11.25 at time of issuance (the “Q3 2018 Warrants”). At the time of issuance, half of these Q3 2018 Warrants had a five-year term and half had a one-year term. In September 2018, the exercise price was modified to \$7.50.

In April 2019, as a result of the Amendment No.2 Agreement, the exercise price of the Q3 2018 Warrants was adjusted to \$5.40 and all Q3 2018 Warrants that had a one-year term were amended to have a five-year term. Due to these modifications, the change in fair value of the Q3 2018 Warrants was calculated to be an expense of approximately \$0.4 million which is included in loss on modification of warrants in the consolidated statements of operations for the nine months ended September 30, 2019. The expense for the three months ended September 30, 2019 was zero.

There were zero and 53,610 Q3 2018 Warrants exercised during the three and nine months ended September 30, 2019, respectively, for proceeds to the Company of zero and approximately \$290,000, respectively. During the nine months ended September 30, 2019, the intrinsic value of the Q3 2018 Warrants exercised was approximately \$133,382.

In connection with the issuance Bridge Notes during the fourth quarter of 2018, the Company issued 300,115 warrants with an exercise price of \$5.40 at time of issuance and a five-year term (the “Q4 2018 Warrants”).

There were zero and 173,045 Q4 2018 Warrants exercised during the three and nine months ended September 30, 2019, respectively, for proceeds to the Company of zero and approximately \$935,000, respectively. During the nine months ended September 30, 2019, the intrinsic value of the Q4 2018 Warrants exercised was approximately \$489,000.

#### April 2019 Warrants

In connection with the issuance of the April 2019 Bridge Notes, the Company issued 147,472 warrants with an exercise price of \$5.40 and a five-year term.

#### May 2019 Warrants

In connection with the issuance of the May 2019 Bridge Notes, the Company issued 154,343 warrants with an exercise price of \$5.40 and a five-year term.

#### *Deemed Dividends*

As discussed above, certain of our preferred stock and warrant issuances contain down round provisions which require us to recognize the effect of the down round feature when it is triggered. That effect is treated as a dividend and as a reduction of income available to common shareholders in basic earnings per share.

There were no deemed dividends during the three months ended September 30, 2020 or the three and nine months ended September 30, 2019. The following represents a summary of the dividends recorded for the nine months ended September 30, 2020:

<b>Deemed Dividends</b>	<b>Amount Recorded</b> (in thousands)
<i>Dividends resulting from the March 2020 Amendment</i>	
Deemed Dividend A	\$ 3,333
Deemed Dividend B	6
Deemed Dividend C	*
Deemed Dividend D	5
<b>For the nine months ended September 30, 2020</b>	<b>\$ 3,344</b>

\* Represents less than one thousand dollars

## **9. FAIR VALUE**

FASB guidance on fair value measurements, which defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements for our financial assets and liabilities, as well as for other assets and liabilities that are carried at fair value on a recurring basis in our condensed consolidated financial statements.

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FASB guidance establishes a three-level fair value hierarchy based upon the assumptions (inputs) used to price assets or liabilities. The three levels of inputs used to measure fair value are as follows:

Level 1—Unadjusted quoted prices in active markets for identical assets or liabilities;

Level 2—Observable inputs other than those included in Level 1, such as quoted prices for similar assets and liabilities in active markets or quoted prices for identical assets or liabilities in inactive markets; and

Level 3—Unobservable inputs reflecting our own assumptions and best estimate of what inputs market participants would use in pricing the asset or liability.

### *Common Stock Warrant Liabilities.*

Certain of our issued and outstanding warrants to purchase shares of common stock do not qualify to be treated as equity and, accordingly, are recorded as a liability. We are required to record these instruments at fair value at each reporting date and changes are recorded as a non-cash adjustment to earnings. The gains or losses included in earnings are reported in other income (expense) in our condensed consolidated statement of operations.

### 2016 Warrant Liability

The Company has a warrant liability related to warrants issued in January 2016 (the “2016 Warrant Liability”) and it represents the fair value of such warrants, of which, 357 warrants remain outstanding as of September 30, 2020.

In March 2018, a portion of the 2016 Warrant Liability was part of a settlement agreement pursuant to a lawsuit that was filed against the Company by one of the warrant holders. As such, approximately \$0.4 million of the warrant liability, representing 1,347 warrants, was canceled on the date of the settlement agreement.

The 2016 Warrant Liability is considered a Level 3 financial instrument and was valued using the Monte Carlo methodology. As of September 30, 2020, assumptions and inputs used in the valuation of the 2016 Warrant Liability include: remaining life to maturity of 0.3 years; annual volatility of 407%; and a risk-free interest rate of 0.09%. As of December 31, 2019, assumptions and inputs used in the valuation of the 2016 Warrant Liability include: remaining life to maturity of one year; annual volatility of 140%; and a risk-free interest rate of 1.59%.

### Bridge Note Warrant Liabilities

During 2018 and 2019, the Company issued warrants in connection with the issuance of Bridge Notes. All of these warrants issuances were classified as warrant liabilities (the “Bridge Note Warrant Liabilities”). See Note 4 - Convertible Notes for further discussion.

The Bridge Note Warrant Liabilities are considered Level 3 financial instruments and were valued using the Black Scholes model. As of September 30, 2020, assumptions used in the valuation of the Bridge Note Warrant Liabilities include: remaining life to maturity of 1.55 to 3.62 years; annual volatility of 168% to 206%; and risk free rate of 0.11% to 0.19%.

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During the three and nine months ended September 30, 2020 and 2019, the change in the fair value of the warrant liabilities measured using significant unobservable inputs (Level 3) were comprised of the following:

**Dollars in Thousands**

	<b>Three Months Ended September 30, 2020</b>		
	<b>2016 Warrant Liability</b>	<b>Bridge Note Warrant Liabilities</b>	<b>Total Warrant Liabilities</b>
Beginning balance at July 1	\$ 39	\$ 735	\$ 774
Total (gains) losses:			
Revaluation recognized in earnings	63	794	857
Balance at September 30	<u>\$ 102</u>	<u>\$ 1,529</u>	<u>\$ 1,631</u>

	<b>Three Months Ended September 30, 2019</b>		
	<b>2016 Warrant Liability</b>	<b>Bridge Note Warrant Liabilities</b>	<b>Total Warrant Liabilities</b>
Beginning balance at July 1	\$ 86	\$ 2,250	\$ 2,336
Total (gains) losses:			
Revaluation recognized in earnings	(7)	(556)	(563)
Balance at September 30	<u>\$ 79</u>	<u>\$ 1,694</u>	<u>\$ 1,773</u>

**Dollars in Thousands**

	<b>Nine Months Ended September 30, 2020</b>		
	<b>2016 Warrant Liability</b>	<b>Bridge Note Warrant Liabilities</b>	<b>Total Warrant Liabilities</b>
Beginning balance at January 1	\$ 70	\$ 1,268	\$ 1,338
Total gains:			
Revaluation recognized in earnings	32	261	293
Balance at September 30	<u>\$ 102</u>	<u>\$ 1,529</u>	<u>\$ 1,631</u>

	<b>Nine Months Ended September 30, 2019</b>		
	<b>2016 Warrant Liability</b>	<b>Bridge Note Warrant Liabilities</b>	<b>Total Warrant Liabilities</b>
Beginning balance at January 1	\$ 116	\$ 1,016	\$ 1,132
Additions:	–	1,858	1,858
Total (gains) losses:			
Revaluation recognized in earnings	(37)	56	19
Modification recognized in earnings	–	1,128	1,128
Deductions – warrant liability settlement	–	(2,364)	(2,364)
Balance at September 30	<u>\$ 79</u>	<u>\$ 1,694</u>	<u>\$ 1,773</u>

*Derivative Liabilities.*

Certain of our issued and outstanding convertible notes contain features that are considered derivative instruments and are required to bifurcated from the debt host and accounted for separately as derivative liabilities. The estimated fair value of the derivatives will be remeasured at each reporting date and any change in estimated fair value of the derivatives will be recorded as non-cash adjustments to earnings. The gains or losses included in earnings are reported in other (expense) income in our condensed consolidated statement of operations.

#### Bridge Notes Redemption Feature

Valuations for derivatives related to Bridge Note redemption features were performed using the “with and without” approach, whereby the Bridge Notes were valued both with the embedded derivative and without.

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#### Conversion Option

Valuations for derivatives related to conversion options were performed using the Monte Carlo methodology.

During the three and nine months ended September 30, 2020 and during the three months ended September 30, 2019, the change in the fair value of the derivative liabilities was zero. During the nine months ended September 30, 2019, the change in the fair value of the derivative liabilities measured using significant unobservable inputs (Level 3) was comprised of the following:

(Dollars in thousands)

	<u>Nine Months Ended September 30, 2019</u>		
	<u>Bridge Notes Redemption Feature</u>	<u>Conversion Option</u>	<u>Total Derivative Liabilities</u>
Beginning balance at January 1	\$ 30	\$ 32	\$ 62
Deductions - write-off in conjunction with convertible note conversions	(438)	(39)	(477)
Total loss:			
Revaluation recognized in earnings	408	7	415
Balance at September 30	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>

## 10. EQUITY INCENTIVE PLAN

The Company currently issues stock awards under its 2017 Stock Option and Incentive Plan, as amended (the "2017 Plan") which will expire on June 5, 2027. Per the terms of the 2017 Plan, the shares authorized for issuance under the 2017 Plan were 913,586 at September 30, 2020, of which 105,433 remain available for future grant. The shares authorized under the 2017 Plan are subject to annual increases on January 1 by 5% of the number of shares of common stock issued and outstanding on the immediately preceding December 31, or such lesser number of shares determined by the Company's Board of Directors or Compensation Committee. During the nine months ended September 30, 2020, the shares authorized for issuance increased by 394,905 shares.

### *Stock Options.*

The Company accounts for all stock-based compensation payments to employees and directors, including grants of employee stock options, at fair value at the date of grant and expenses the benefit in operating expense in the condensed consolidated statements of operations over the service period of the awards. The Company records the expense for stock-based compensation awards subject to performance-based milestone vesting over the remaining service period when management determines that achievement of the milestone is probable based on the expected satisfaction of the performance conditions as of the reporting date. The fair value of each stock option granted is estimated on the date of grant using the Black-Scholes option pricing model, which requires various assumptions including estimating stock price volatility, expected life of the stock option, risk free interest rate and estimated forfeiture rate.

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During the nine months ended September 30, 2020, the Company granted stock options to purchase up to 393,050 shares of common stock at a weighted average exercise price of \$1.99. The following table summarizes stock option activity under our plans during the nine months ended September 30, 2020:

	<b>Number of Options</b>	<b>Weighted-Average Exercise Price</b>
Outstanding at January 1, 2020	490,330	\$ 8.30
Granted	393,050	1.99
Forfeited	(75,135)	13.86
Outstanding at September 30, 2020	<u>808,245</u>	<u>\$ 4.72</u>
Exercisable at September 30, 2020	<u>335,493</u>	<u>\$ 7.03</u>

As of September 30, 2020, there were 690,057 options that were vested or expected to vest with an aggregate intrinsic value of \$0.2 million and a remaining weighted average contractual life of 8.5 years.

During the nine months ended September 30, 2019, there were 285,364 options granted with a weighted average exercise price of \$2.37 and 16,351 options forfeited with a weighted average exercise price of \$7.22.

For the three and nine months ended September 30, 2020, we recorded compensation expense for all stock awards of \$0.2 million and \$0.5 million, respectively, within operating expense in the accompanying statements of operations. For the three and nine months ended September 30, 2019, we recorded compensation expense for all stock awards of \$0.2 million and \$0.5 million, respectively. As of September 30, 2020, the unrecognized compensation expense related to unvested stock awards was \$1.7 million, which is expected to be recognized over a weighted-average period of 1.8 years.

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## **11. SALES SERVICE REVENUE, NET AND ACCOUNTS RECEIVABLE**

### *ASC Topic 606, "Revenue from contracts with customers"*

The Company follows the guidance of ASC 606 for the recognition of revenue from contracts with customers to transfer goods and services. The Company performed a comprehensive review of its existing revenue arrangements following the five-step model:

Step 1: Identification of the contract with the customer. Sub-steps include determining the customer in a contract; Initial contract identification and determine if multiple contracts should be combined and accounted for as a single transaction.

Step 2: Identify the performance obligation in the contract. Sub-steps include identifying the promised goods and services in the contract and identifying which performance obligations within the contract are distinct.

Step 3: Determine the transaction price. Sub-steps include variable consideration, constraining estimates of variable consideration, the existence of a significant financing component in the contract, noncash consideration and consideration payable to a customer.

Step 4: Allocate transaction price. Sub-steps include assessing the amount of consideration to which the Company expects to be entitled in exchange for transferring the promised goods or services to the customer.

Step 5: Satisfaction of performance obligations. Sub-steps include ascertaining the point in time when an asset is transferred to the customer and the customer obtains control of the asset upon which time the Company recognizes revenue.

#### *Nature of Contracts and Customers*

The Company's contracts and related performance obligations are similar for its customers and the sales process for all customers starts upon the receipt of requisition forms from the customers for patient diagnostic testing



and the execution of contracts for biomarker testing and clinical research. Payment terms for the services provided are 30 days, unless separately negotiated.

*Diagnostic testing*

Control of the laboratory testing services is transferred to the customer at a point in time. As such, the Company recognizes revenue for laboratory testing services at a point in time based on the delivery method (web-portal access or fax) for the patient’s laboratory report, per the contract.

*Clinical research grants*

Control of the clinical research services are transferred to the customer over time. The Company will recognize revenue utilizing the “effort based” method, measuring its progress toward complete satisfaction of the performance obligation.

*Biomarker testing and clinical project services*

Control of the biomarker testing and clinical project services are transferred to the customer over time. The Company utilizes an “effort based” method of assessing performance and measures progress towards satisfaction of the performance obligation based upon the delivery of results.

The Company generates revenue from the provision of diagnostic testing provided to patients, biomarker testing provided to bio-pharma customers and clinical research grants funded by both bio-pharma customers and government health programs.

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*Disaggregation of Revenues by Transaction Type*

We operate in one business segment and, therefore, the results of our operations are reported on a consolidated basis for purposes of segment reporting, consistent with internal management reporting. Service revenue, net for the three and nine months ended September 30, 2020 and 2019 were as follows (prior-period amounts are not adjusted under the modified-retrospective method of adoption):

(dollars in thousands)	For the Three Months Ended September 30,					
	Diagnostic Testing		Biomarker Testing		Total	
	2020	2019	2020	2019	2020	2019
Medicaid	\$ 15	\$ 10	\$ —	\$ —	\$ 15	\$ 10
Medicare	811	373	—	—	811	373
Self-pay	196	5	—	—	196	5
Third party payers	950	490	—	—	950	490
Contract diagnostics	—	—	26	142	26	142
Service revenue, net	<u>\$ 1,972</u>	<u>\$ 878</u>	<u>\$ 26</u>	<u>\$ 142</u>	<u>\$ 1,998</u>	<u>\$ 1,020</u>

(dollars in thousands)	For the Nine Months Ended September 30,					
	Diagnostic Testing		Biomarker Testing		Total	
	2020	2019	2020	2019	2020	2019
Medicaid	\$ 40	\$ 22	\$ —	\$ —	\$ 40	\$ 22
Medicare	1,979	1,217	—	—	1,979	1,217
Self-pay	332	20	—	—	332	20
Third party payers	2,313	1,297	—	—	2,313	1,297
Contract diagnostics	—	—	408	569	408	569
Service revenue, net	<u>\$ 4,664</u>	<u>\$ 2,556</u>	<u>\$ 408</u>	<u>\$ 569</u>	<u>\$ 5,072</u>	<u>\$ 3,125</u>

Revenue from the Medicare and Medicaid programs account for a portion of the Company's patient diagnostic service revenue. Laws and regulations governing those programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

#### *Revenue Recognition*

Revenue is recognized when a customer obtains control of promised goods or services, in an amount that reflects the consideration which the entity expects to receive in exchange for those goods or services. To the extent the transaction price includes variable consideration, the Company estimates the amount of variable consideration that should be included in the transaction price using the expected value method based on historical experience. The Company does not typically enter arrangements where multiple contracts can be combined as the terms regarding services are generally found within a single agreement/requisition form. The Company derives its revenues from three types of transactions: diagnostic testing ("Diagnostic"), and clinical research grants from state and federal research programs, and other revenues from the Company's ICP technology and bio-pharma projects encompassing genetic diagnostics (collectively "Biomarker").

#### *Deferred revenue*

Deferred revenue, or unearned revenue, refers to advance payments for products or services that are to be delivered in the future. The Company records such prepayment of unearned revenue as a liability, as revenue that has not yet been earned, but represents products or services that are owed to a customer. As the product or service is delivered over time, the Company recognizes the appropriate amount of revenue from deferred revenue. For the period ended September 30, 2020 and December 31, 2019, the deferred revenue was \$48,000 and \$35,000, respectively.

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#### *Contractual Allowances and Adjustments*

We are reimbursed by payers for services we provide. Payments for services covered by payers average less than billed charges. We monitor revenue and receivables from payers and record an estimated contractual allowance for certain revenue and receivable balances as of the revenue recognition date to properly account for anticipated differences between amounts estimated in our billing system and amounts ultimately reimbursed by payers.

Accordingly, the total revenue and receivables reported in our condensed consolidated financial statements are recorded at the amounts expected to be received from these payers. For service revenue, the contractual allowance is estimated based on several criteria, including unbilled claims, historical trends based on actual claims paid, current contract and reimbursement terms and changes in customer base and payer/product mix. The billing functions for the remaining portion of our revenue are contracted and fixed fees for specific services and are recorded without an allowance for contractual discounts. The following table presents our revenues initially recognized for each associated payer class during the three and nine months ended September 30, 2020 and 2019.

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(dollars in thousands)	For the Three Months Ended September 30,					
	Gross Revenues		Contractual Allowances and adjustments		Revenues, net of Contractual Allowances and adjustments	
	2020	2019	2020	2019	2020	2019
Medicaid	\$ 15	\$ 10	\$ —	\$ —	\$ 15	\$ 10
Medicare	811	373	—	—	811	373
Self-pay	196	5	—	—	196	5
Third party payers	3,188	1,701	(2,238)	(1,211)	950	490
Contract diagnostics	26	142	—	—	26	142
	<u>4,236</u>	<u>2,231</u>	<u>(2,238)</u>	<u>(1,211)</u>	<u>1,998</u>	<u>1,020</u>
Clinical research grants and other	51	26	—	—	51	26
	<u>\$4,287</u>	<u>\$2,257</u>	<u>\$ (2,238)</u>	<u>\$ (1,211)</u>	<u>\$ 2,049</u>	<u>\$ 1,046</u>

(dollars in thousands)	For the Nine Months Ended September 30,					
	Gross Revenues		Contractual Allowances and adjustments		Revenues, net of Contractual Allowances and adjustments	
	2020	2019	2020	2019	2020	2019
Medicaid	\$ 40	\$ 25	\$ —	\$ (3)	\$ 40	\$ 22
Medicare	1,979	1,234	—	(17)	1,979	1,217
Self-pay	335	20	(3)	—	332	20
Third party payers	7,944	4,289	(5,631)	(2,992)	2,313	1,297
Contract diagnostics	408	569	—	—	408	569
	<u>10,706</u>	<u>6,137</u>	<u>(5,634)</u>	<u>(3,012)</u>	<u>5,072</u>	<u>3,125</u>
Clinical research grants and other	104	37	—	—	104	37
	<u>\$10,810</u>	<u>\$6,174</u>	<u>\$ (5,634)</u>	<u>\$ (3,012)</u>	<u>\$ 5,176</u>	<u>\$ 3,162</u>

*Allowance for Doubtful Accounts*

The Company provides for a general allowance for collectability of services when recording net sales. The Company has adopted the policy of recognizing net sales to the extent it expects to collect that amount. Reference FASB 954-605-45-5 and ASU 2011-07, Health Care Entities: Presentation and Disclosure of Patient Service Revenue,

Provision for Bad Debt, and the Allowance for Doubtful Accounts. The change in the allowance for doubtful accounts is directly related to the increase in patient service revenues. The following table presents our reported revenues net of the collection allowance and adjustments for the three and nine months ended September 30, 2020 and 2019.

<b>For the Three Months Ended September 30,</b>						
(dollars in thousands)	<b>Revenues, net of</b>		<b>Contractual Allowances</b>		<b>Allowances for doubtful</b>	
	<b>and adjustments</b>		<b>accounts</b>		<b>Total</b>	
	<b>2020</b>	<b>2019</b>	<b>2020</b>	<b>2019</b>	<b>2020</b>	<b>2019</b>
Medicaid	\$ 15	\$ 10	\$ (15)	\$ (10)	\$ —	\$ —
Medicare	811	373	(121)	(56)	690	317
Self-pay	196	5	—	—	196	5
Third party payers	950	490	(286)	(196)	664	294
Contract diagnostics	26	142	—	—	26	142
	1,998	1,020	(422)	(262)	1,576	758
Clinical research grants and other	51	26	—	—	51	26
	<u>\$ 2,049</u>	<u>\$ 1,046</u>	<u>\$ (422)</u>	<u>\$ (262)</u>	<u>\$ 1,627</u>	<u>\$ 784</u>

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<b>For the Nine Months Ended September 30,</b>						
(dollars in thousands)	<b>Revenues, net of</b>		<b>Contractual Allowances</b>		<b>Allowances for doubtful</b>	
	<b>and adjustments</b>		<b>accounts</b>		<b>Total</b>	
	<b>2020</b>	<b>2019</b>	<b>2020</b>	<b>2019</b>	<b>2020</b>	<b>2019</b>
Medicaid	\$ 40	\$ 22	\$ (40)	\$ (22)	\$ —	\$ —
Medicare	1,979	1,217	(296)	(183)	1,683	1,034
Self-pay	332	20	—	—	332	20
Third party payers	2,313	1,297	(689)	(518)	1,624	779
Contract diagnostics	408	569	—	—	408	569
	5,072	3,125	(1,025)	(723)	4,047	2,402
Clinical research grants and other	104	37	—	—	104	37
	<u>\$ 5,176</u>	<u>\$ 3,162</u>	<u>\$ (1,025)</u>	<u>\$ (723)</u>	<u>\$ 4,151</u>	<u>\$ 2,439</u>

*Costs to Obtain or Fulfill a Customer Contract*

Sales commissions are expensed when incurred because the amortization period would have been one year or less. These costs are recorded in operating expenses in the condensed consolidated statements of operations.

Shipping and handling costs are comprised of inbound and outbound freight and associated labor. The Company accounts for shipping and handling activities related to contracts with customers as fulfillment costs which are included in cost of sales in the condensed consolidated statements of operations.

Accounts Receivable

The Company has provided an allowance for potential credit losses, which has been determined based on management's industry experience. The Company grants credit without collateral to its patients, most of who are insured under third party payer agreements.

The following summarizes the mix of receivables:

(dollars in thousands)	<u>September 30, 2020</u>	<u>December 31, 2019</u>
Medicaid	\$ 132	\$ 107
Medicare	1,002	814
Self-pay	403	88
Third party payers	3,211	2,203
Contract diagnostic services	37	36
	<u>\$ 4,785</u>	<u>\$ 3,248</u>
Less allowance for doubtful accounts	(3,699)	(2,674)
Accounts receivable, net	<u>\$ 1,086</u>	<u>\$ 574</u>

The following table presents the roll-forward of the allowance for doubtful accounts for the nine months ended September 30, 2020.

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(dollars in thousands)	<u>Allowance for Doubtful Accounts</u>
Balance, January 1, 2020	\$ (2,674)
Collection Allowance:	
Medicaid	\$ (40)
Medicare	(296)
Third party payers	<u>(689)</u>
	(1,025)
Bad debt expense	<u>\$ —</u>
Total charges	(1,025)
Balance, September 30, 2020	<u>\$ (3,699)</u>

### Customer Revenue and Accounts Receivable Concentration

Customers that accounted for 10% or greater of our net sales or accounts receivable for the identified periods is as follows:

	Net sales				Accounts receivable, as of	
	Three Months Ended		Nine Months Ended		September 30,	December 31,
	September 30,		September 30,			
2020	2019	2020	2019	2020	2019	
Customer A	*	18 %	*	23 %	*	*
Customer B	*	11 %	*	*	*	17 %
Customer C	*	*	*	*	10 %	12 %
Customer D	*	*	*	*	10 %	*

\* represents less than 10%

## 12. SUBSEQUENT EVENTS

The Company has evaluated events and transactions subsequent to September 30, 2020 through the date the condensed consolidated financial statements were issued and there are no other events to report other than what has been disclosed in the condensed consolidated financial statements.

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## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

### Forward-Looking Information

This Quarterly Report on Form 10-Q, including this Management's Discussion and Analysis, contains forward-looking statements. These statements are based on management's current views, assumptions or beliefs of future events and financial performance and are subject to uncertainty and changes in circumstances. Readers of this report should understand that these statements are not guarantees of performance or results. Many factors could affect our actual financial results and cause them to vary materially from the expectations contained in the forward-looking statements. These factors include, among other things: the expected or potential impact of COVID-19 which is highly uncertain and will depend on future developments, our expected revenue, income (loss), receivables, operating expenses, supplier pricing, availability and prices of raw materials, insurance reimbursements, product pricing, sources of funding operations, our ability to raise funds, sufficiency of available liquidity, future interest costs, future economic

circumstances, business strategy, industry conditions, our ability to execute our operating plans, the success of our cost savings initiatives, competitive environment and related market conditions, expected financial and other benefits from our organizational restructuring activities, actions of governments and regulatory factors affecting our business, retaining key employees and other risks as described in our reports filed with the Securities and Exchange Commission. In some cases these statements are identifiable through the use of words such as “anticipate,” “believe,” “estimate,” “expect,” “intend,” “plan,” “project,” “target,” “can,” “could,” “may,” “should,” “will,” “would” or the negative versions of these terms and other similar expressions.

You are cautioned not to place undue reliance on these forward-looking statements. The forward-looking statements we make are not guarantees of future performance and are subject to various assumptions, risks and other factors that could cause actual results to differ materially from those suggested by these forward-looking statements. Actual results may differ materially from those suggested by the forward-looking statements that we make for a number of reasons, including those described in Part II, Item 1A, “Risk Factors,” of this Quarterly Report on Form 10-Q and our prior filings with the Securities and Exchange Commission.

We expressly disclaim any obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.

The following discussion should be read together with our condensed consolidated financial statements and related notes contained in this Quarterly Report on Form 10-Q and with the financial statements, related notes and Management’s Discussion and Analysis included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2019, which we filed with the Securities and Exchange Commission on March 27, 2020. Results for the three and nine months ended September 30, 2020 are not necessarily indicative of results that may be attained in the future.

## **Overview**

We are a cancer diagnostics company providing diagnostic products and services to the oncology market. We have built and continue to develop a platform designed to eradicate the problem of misdiagnosis by harnessing the intellect, expertise and technologies developed within academic institutions, and delivering quality diagnostic information to physicians and their patients worldwide. We operate a cancer diagnostic laboratory located in New Haven, Connecticut and have partnered with various academic institutions to capture the expertise, experience and technologies developed within academia to provide a better standard of cancer diagnostics and aim to solve the growing problem of cancer misdiagnosis. We also operate a research and development facility in Omaha, Nebraska which focuses on development of various technologies, among them IV-Cell, HemeScreen and ICE-COLD-PCR, or ICP, the patented technology described further below, which we exclusively licensed from Dana-Farber Cancer Institute, Inc., or Dana-Farber, at Harvard University. The research and development center focuses on the development of these technologies, which we believe will enable us to commercialize these and other technologies developed with our current and future academic partners. The facility in Omaha was also recently certified as a CLIA and CAP facility, and we have begun bringing in house several

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molecular tests that the Company had previously referenced out to other laboratories. Our platform also connects patients, physicians and diagnostic experts residing within academic institutions.

In April 2020, we formed the Joint Venture with Poplar. Poplar provides specialized laboratory testing services to a nationwide client base of gastroenterologists, dermatologists, oncologists, urologists, gynecologists and their patients. The business purpose of the Joint Venture is to facilitate and capitalize on the combined capabilities, resources and healthcare industry relationships of its members by partnering, promoting and providing oncology services to office based physicians, hospitals and medical centers. Under the terms of the Joint Venture, Precipio SPV has a 49% ownership interest in the Joint Venture, with Poplar having a 51 % ownership. We have determined that we hold a variable interest in the Joint Venture and that we are the primary beneficiary of the Joint Venture. Due to this determination, we consolidate the Joint Venture. See Note 2 - Summary of Significant Accounting Policies for further discussion.

## **Recent Developments**

### *Business Activities*

During the second quarter of 2020, we launched our new HemeScreen Reagent Rental (HSRR) program. The HSRR program enables us to offer our patent-pending HemeScreen technology beyond the laboratory and into the oncologist's office. Through this program, the physician practice will have testing equipment in their facility with the ability to run diagnostic tests in-house instead of sending out to reference laboratories, obtaining faster results and providing patients with better care. During the third quarter of 2020, we continued the roll out of the HSRR program as we began installation and validation of equipment at our first HSSR customer and signed up a couple more customers to the program. We expect revenues from these customers to begin in the fourth quarter 2020.

On July 30, 2020, the Company announced that it entered into an agreement with ADS Biotec, a US company based in Omaha, Nebraska, to distribute its FDA-authorized COVID-19 serology antibody tests that recently received EUA (Emergency Use Authorization). Distribution of the product will take place in the US as well as in other markets worldwide. During the third quarter of 2020 we began rolling out these antibody tests as CLIA tests run in our laboratory. Further, we plan on rolling out, pending further FDA authorization, antibody tests to physician offices as a POC (point-of-care) tests; as well as, through distribution via various retail channels for at-home, DTC (direct-to-consumer) use.

### Virus vs. Antibody test

While both the active virus and antibody tests are important elements of controlling the pandemic, antibody testing is key to enabling society to return to full functionality. The antibody test for IgM and IgG detects the body's immune response to the infection caused by the virus. As stated by the FDA, antibody tests could play a role in the fight against COVID-19 by helping healthcare professionals identify individuals who may have developed an immune response to the SARS-CoV-2 virus. This is a key to returning our children to schools, adults to work, opening up the economy and resuming life as we knew it prior to the pandemic.

## **Going Concern**

The condensed consolidated financial statements have been prepared using accounting principles generally accepted in the United States of America ("GAAP") applicable for a going concern, which assume that the Company will realize its assets and discharge its liabilities in the ordinary course of business. The Company has incurred substantial operating losses and has used cash in its operating activities for the past several years. As of September 30, 2020, the Company had a net loss of \$8.7 million, negative working capital of \$0.5 million and net cash used in operating activities of \$6.0 million. The Company's ability to continue as a going concern over the next twelve months from the date of issuance of this Quarterly Report on Form 10-Q is dependent upon a combination of achieving its business plan, including generating additional revenue and avoiding potential business disruption due to COVID-19, and raising additional financing to meet its debt obligations and paying liabilities arising from normal business operations when they come due.



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To meet its current and future obligations the Company has taken the following steps to capitalize the business and successfully achieve its business plan:

- On March 26, 2020, the Company entered into the LP 2020 Purchase Agreement, pursuant to which Lincoln Park has agreed to purchase from the Company up to an aggregate of \$10.0 million of common stock of the Company (subject to certain limitations) from time to time over the term of the LP 2020 Purchase Agreement. The extent we rely on Lincoln Park as a source of funding will depend on a number of factors including, the prevailing market price of our common stock and the extent to which we are able to secure working capital from other sources. As of the date of issuance of this Quarterly Report on Form 10-Q, we have already received \$6.7 million from the LP 2020 Purchase Agreement from the sale of 4,130,000 shares of common stock to Lincoln Park from April 1, 2020 through the date of issuance of this Form 10-Q, leaving the Company an additional \$3.3 million to draw subsequent to the filing of this Quarterly Report. See Note 8 Stockholders' Equity for further discussion on Lincoln Park agreements; and
- The Company filed with the SEC a registration statement on Form S-3 on March 27, 2020, as amended on April 9, 2020, to register an indeterminate number of shares of common stock and preferred stock, such indeterminate principal amount of debt securities and such indeterminate number of warrants to purchase common stock, preferred stock or debt securities as shall have an aggregate initial offering price not to exceed \$50 million. This registration statement was declared effective by the SEC on April 13, 2020 and allows the Company, from time to time, to offer up to \$50 million of any combination of the securities described in the Form S-3 in one or more offerings. In order for the Company to utilize the effective S-3, it will have to file subsequent prospectus supplement(s) with regard to the securities it will offer, as applicable from time to time. As of the date of issuance of this Form 10-Q, no subsequent prospectus supplements to this effect have been filed by the Company.

Notwithstanding the aforementioned circumstances, there remains substantial doubt about the Company's ability to continue as a going concern over the next twelve months from the date of issuance of this Quarterly Report on Form 10-Q. There can be no assurance that the Company will be able to successfully achieve its initiatives summarized above in order to continue as a going concern. The accompanying condensed consolidated financial statements have been prepared assuming the Company will continue as a going concern and do not include any adjustments that might result should the Company be unable to continue as a going concern as a result of the outcome of this uncertainty.

### **Outlook - COVID-19 related**

The COVID-19 outbreak, which spread worldwide in the first quarter of 2020, has caused significant business disruption. The extent of the impact of COVID-19 on the Company's operational and financial performance will depend on certain developments, including the duration and spread of the outbreak, and impact on the Company's customers, employees and vendors, all of which are uncertain and cannot be predicted. These uncertainties could have a material adverse effect on our business, financial condition or results of operations. We have been actively monitoring the COVID-19 situation and its impact on the global economy and the Company. As the global pandemic evolves, we will continue to monitor the extent to which COVID-19 impacts our revenues, expenses and liquidity.

[Table of Contents](#)**Results of Operations for the Three Months Ended September 30, 2020 and 2019**

*Net Sales.* Net sales were as follows:

	Dollars in Thousands			
	Three Months Ended		Change	
	September 30,			
	2020	2019	\$	%
Service revenue, net, less allowance for doubtful accounts	\$ 1,576	\$ 758	\$ 818	108 %
Other	51	26	25	96 %
Net Sales	<u>\$ 1,627</u>	<u>\$ 784</u>	<u>\$ 843</u>	<u>108 %</u>

Net sales for the three months ended September 30, 2020 were approximately \$1.6 million, an increase of \$0.8 million as compared to the same period in 2019. During the three months ended September 30, 2020, service revenue, less allowance for doubtful accounts, increased due to patient diagnostic service revenue which had an increase of \$0.9 million as compared to the same period in 2019 due to an increase in cases processed. We processed 1,135 cases during the three months ended September 30, 2020 as compared to 445 cases during the same period in 2019, or a 155% increase in cases. The increase in volume is the result of increased sales personnel. The increase in patient diagnostic service revenue was partially offset by a decrease of \$0.1 million in contract diagnostics revenue for the three months ended September 30, 2020 as compared to the same period in 2019. Other revenue increased less than \$0.1 million for the three months ended September 30, 2020 as compared to the same period in 2019.

*Cost of Sales.* Cost of sales includes material and supply costs for the patient tests performed and other direct costs (primarily personnel costs and rent) associated with the operations of our laboratory and the costs of projects related to clinical research grants (personnel costs and operating supplies). Cost of sales was \$1.2 million and \$0.8 million for the three months ended September 30, 2020 and 2019, respectively. Cost of sales in the current year period, as compared to prior year, included an increase in patient diagnostic costs, partially offset by a decrease in contract diagnostic costs, which are in line with the changes in related revenues discussed above.

*Gross Profit.* Gross profit and gross margins were as follows:

	Dollars in Thousands			
	Three Months Ended		Margin %	
	September 30,			
	2020	2019	2020	2019
Gross Profit	<u>\$ 377</u>	<u>\$ 28</u>	<u>23 %</u>	<u>4 %</u>

Gross margin was 23% of total net sales, for the three months ended September 30, 2020, compared to 4% of total net sales for the same period in 2019. The gross profit was \$0.4 million and less than \$0.1 million during the three months ended September 30, 2020 and 2019, respectively. The gross margin increased during the three months ended September 30, 2020, as compared to the prior year period, as a result of increases in case volume and revenue. The increase in case volume allowed our laboratory to absorb the excess capacity of its technician labor and enabled us to leverage fixed expenses.

*Operating Expenses.* Operating expenses primarily consist of personnel costs, professional fees, travel costs, facility costs and depreciation and amortization. Our operating expenses increased by \$0.4 million to \$2.8 million for the three months ended September 30, 2020 as compared to the same period in 2019. This increase includes a \$0.3

million increase in sales and marketing costs, which is primarily increased personnel costs related to our increase in patient diagnostic service revenues, an increase of \$0.1 million in general and administrative personnel costs and an increase of \$0.1 million in stock based compensation costs. These increases were partially offset by a decrease of \$0.1 million in general and administrative professional fees.

*Other (Expense) Income.* We recorded other expense, net of \$0.9 million and other income, net of \$0.5 million for the three months ended September 30, 2020 and 2019, respectively. The current year period net expense of \$0.9 million

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is expense recorded on warrant revaluations. During the three months ended September 30, 2019, other income, net of \$0.5 million included income from warrant revaluations of \$0.6 million, which was partially offset by \$0.1 million of interest expense. The warrant revaluations are directly impacted by, among other things, the change in our stock price from one reporting date to the next. See Note 9 – Fair Value for further discussion on warrant liability valuations.

**Results of Operations for the Nine Months Ended September 30, 2020 and 2019**

*Net Sales.* Net sales were as follows:

	Dollars in Thousands			
	Nine Months Ended		Change	
	September 30,			
	2020	2019	\$	%
Service revenue, net, less allowance for doubtful accounts	\$ 4,047	\$ 2,402	\$ 1,645	68 %
Other	104	37	67	181 %
Net Sales	<u>\$ 4,151</u>	<u>\$ 2,439</u>	<u>\$ 1,712</u>	<u>70 %</u>

Net sales for the nine months ended September 30, 2020 were approximately \$4.2 million, an increase of \$1.7 million as compared to the same period in 2019. During the nine months ended September 30, 2020, service revenue, less allowance for doubtful accounts, increased due to patient diagnostic service revenue which had an increase of \$1.8 million as compared to the same period in 2019 due to an increase in cases processed. We processed 2,575 cases during the nine months ended September 30, 2020 as compared to 1,250 cases during the same period in 2019, or a 106% increase in cases. The increase in volume is the result of increased sales personnel. Other revenues increased approximately \$0.1 million. These revenue increases were partially offset by a decrease of \$0.2 million in contract diagnostics revenue for the nine months ended September 30, 2020 as compared to the same period in 2019.

*Cost of Sales.* Cost of sales includes material and supply costs for the patient tests performed and other direct costs (primarily personnel costs and rent) associated with the operations of our laboratory and the costs of projects related to clinical research grants (personnel costs and operating supplies). Cost of sales was \$3.5 million and \$2.2 million for the nine months ended September 30, 2020 and 2019, respectively. Cost of sales in the current year period, as compared to prior year, included an increase in patient diagnostic costs, partially offset by a decrease in contract diagnostic costs, which are in line with the changes in related revenues discussed above.

*Gross Profit.* Gross profit and gross margins were as follows:

	Dollars in Thousands			
	Nine Months Ended		Margin %	
	September 30,			
	2020	2019	2020	2019
Gross Profit	\$ 673	238	16 %	10 %

Gross margin was 16% of total net sales, for the nine months ended September 30, 2020, compared to 10% of total net sales for the same period in 2019. The gross profit was \$0.7 million and \$0.2 million during the nine months ended September 30, 2020 and 2019, respectively. The gross margin increased during the nine months ended September 30, 2020, as compared to the prior year period, as a result of increases in case volume and revenue. The increase in case volume allowed our laboratory to absorb the excess capacity of its technician labor and enabled us to leverage fixed expenses.

*Operating Expenses.* Operating expenses primarily consist of personnel costs, professional fees, travel costs, facility costs and depreciation and amortization. Our operating expenses increased by \$0.6 million to \$7.6 million for the nine months ended September 30, 2020 as compared to the same period in 2019. The increase includes an increase of \$0.8 million in sales and marketing costs, which are primarily increased personnel costs related to our increase in patient

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diagnostic service revenues, and an increase of \$0.1 million in stock based compensation costs. The increases were partially offset by a decrease of \$0.3 million in general and administrative professional fees.

*Other (Expense) Income.* We recorded other expense, net of \$1.8 million and \$2.7 million for the nine months ended September 30, 2020 and 2019, respectively. The current year period net expense of \$1.8 million includes \$0.3 million of interest expense from the amortization of debt discounts, net of accretion of debt premiums, related to convertible notes, \$0.2 million of other interest expense, \$1.2 million in expense for loss on extinguishment of convertible notes which was recorded in conjunction with the March 2020 Amendment and \$0.3 million of expense recorded on warrant revaluations. The expenses were partially offset by \$0.2 million of other income. Approximately \$0.1 million of the other income is funds we received from the U.S. Department of Health and Human Services (“HHS”). As part of the CARES Act, HHS distributed funds to healthcare providers that received Medicare fee-for-service reimbursements in 2019. The payments from HHS are not loans and will not be required to be repaid.

During the nine months ended September 30, 2019, other expense, net of \$2.7 million included expense from warrant and derivative revaluations of \$1.5 million, a loss on issuance of convertible notes of \$1.9 million, a loss on litigation of \$0.3 million and net interest expense of approximately \$0.3 million. These expense items were partially offset by gains on settlements of liabilities of \$1.3 million.

**Liquidity and Capital Resources**

Our working capital positions were as follows:

	Dollars in Thousands		
	September 30, 2020	December 31, 2019	Change
Current assets (including cash of \$2,158 and \$848 respectively)	\$ 3,968	\$ 1,878	\$2,090
Current liabilities	4,467	4,334	133
Working capital	\$ (499)	\$ (2,456)	\$1,957

During the nine months ended September 30, 2020 we received gross proceeds of \$6.9 million from sale of 4,870,654 shares of our common stock. We also converted \$2.2 million of convertible notes, including interest, into 3,908,145 shares of our common stock.

#### **Analysis of Cash Flows – Nine Months Ended September 30, 2020 and 2019**

*Net Change in Cash.* Cash increased by \$1.3 million during the nine months ended September 30, 2020 and 2019, respectively.

*Cash Flows Used in Operating Activities.* The cash flows used in operating activities of approximately \$6.0 million during the nine months ended September 30, 2020 included a net loss of \$8.7 million, an increase in accounts receivable of \$1.5 million, an increase in inventories and other assets of \$0.3 million and a decrease in accounts payable and operating lease liabilities of \$0.3 million. These were partially offset by an increase in accrued expenses and other liabilities of \$0.4 million and non-cash adjustments of \$4.4 million. The non-cash adjustments to net loss include, among other things, depreciation and amortization, changes in provision for losses on doubtful accounts, warrant revaluations, stock based compensation, and loss on extinguishment of convertible notes. The cash flows used in operating activities in the nine months ended September 30, 2019 included the net loss of \$9.5 million, an increase in accounts receivable of \$0.7 million, a decrease in accounts payable of \$1.6 million and a decrease in operating lease liabilities of \$0.2 million. These were partially offset by a decrease in other assets of \$0.3 million and non-cash adjustments of \$4.7 million.

*Cash Flows Used In Investing Activities.* Cash flows used in investing activities were less than \$0.1 million for the nine months ended September 30, 2020 and 2019, respectively, resulting from purchases of property and equipment partially offset by proceeds from sales of fixed assets.

*Cash Flows Provided by Financing Activities.* Cash flows provided by financing activities totaled \$7.4 million for the nine months ended September 30, 2020, which included proceeds of \$6.9 million from the issuance of common

stock and proceeds of \$0.8 million from the PPP Loan. These proceeds were partially offset by payments on our long-term debt and finance lease obligations of \$0.3 million. Cash flows provided by financing activities totaled \$8.4 million for the nine months ended September 30, 2019, which included proceeds of \$5.2 million from the issuance of common stock, \$1.6 million from the exercise of warrants and \$2.1 million from the issuance of convertible notes.

These proceeds were partially offset by payments on our long-term debt and convertible notes of \$0.4 million and payments for our finance lease obligations and deferred financing costs of \$0.1 million.

### **Off-Balance Sheet Arrangements**

At each of September 30, 2020 and December 31, 2019, we did not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

### **Contractual Obligations and Commitments**

No significant changes to contractual obligations and commitments occurred during the nine months ended September 30, 2020, as compared to those disclosed in our Annual Report on Form 10-K for the fiscal year ended December 31, 2019, filed with the Securities and Exchange Commission on March 27, 2020.

### **Critical Accounting Policies and Estimates**

Accounting policies used in the preparation of our financial statements may involve the use of management judgments and estimates. Certain of our accounting policies are considered critical as they are both important to the portrayal of our financial statements and require significant or complex judgments on the part of management. Our judgments and estimates are based on experience and assumptions that we believe are reasonable under the circumstances. Further, we evaluate our judgments and estimates from time to time as circumstances change. Actual financial results based on judgments or estimates may vary under different assumptions or circumstances. Our critical accounting policies are discussed in our Annual Report on Form 10-K for the fiscal year ended December 31, 2019, filed with the Securities and Exchange Commission on March 27, 2020.

### **Recently Issued Accounting Pronouncements**

See the accompanying unaudited condensed consolidated financial statements and Note 2 - "Summary of Significant Accounting Policies" in the Notes to unaudited condensed financial statements for additional information regarding recently issued accounting pronouncements.

### **Impact of Inflation**

We do not believe that price inflation or deflation had a material adverse effect on our financial condition or results of operations during the periods presented.

### **Item 3. Quantitative and Qualitative Disclosure about Market Risk**

We are a smaller reporting company, as defined by Rule 12b-2 of the Securities Exchange Act of 1934, as amended, and are not required to provide the information required under this item.

### **Item 4. Controls and Procedures**

#### *Evaluation of Disclosure Controls and Procedures*

As of the end of the period covered by this Quarterly Report on Form 10-Q, management performed, with the participation of our Chief Executive Officer and Chief Financial Officer, an evaluation of the effectiveness of our disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Our disclosure controls and procedures are designed to provide reasonable assurance

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that information required to be disclosed in the reports we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission (the “SEC”), and that such information is accumulated and communicated to management including our Chief Executive Officer and our Chief Financial Officer, to allow timely decisions regarding required disclosures. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and no evaluation of controls and procedures can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected. Management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective at a reasonable assurance level as of September 30, 2020.

*Changes in Internal Control over Financial Reporting*

We have evaluated the changes in our internal control over financial reporting that occurred during the three months ended September 30, 2020 and concluded that there have not been any changes that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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**PART II. OTHER INFORMATION**

**Item 1. Legal Proceedings**

CPA Global provides us with certain patent management services. On February 6, 2017, CPA Global claimed that we owed approximately \$0.2 million for certain patent maintenance services rendered. CPA Global has not filed claims against us in connection with this allegation. A liability of less than \$0.1 million has been recorded and is reflected in accounts payable within the accompanying condensed consolidated balance sheets at September 30, 2020 and December 31, 2019.

On February 17, 2017, Jesse Campbell (“Campbell”) filed a lawsuit individually and on behalf of others similarly situated against us in the District Court for the District of Nebraska alleging we had a materially incomplete and misleading proxy relating to a potential merger and that the merger agreement’s deal protection provisions deter superior offers. On June 21, 2019, the parties filed a stipulation of settlement, in which defendants are released from all claims and expressly deny that they have committed any act or omission giving rise to any liability. The stipulation includes a settlement payment of \$1.95 million. On July 10, 2019, the Court entered an order preliminarily approving the settlement. During the third quarter of 2019, both the Company and its insurance company paid their

respective amounts of \$0.27 million and \$1.68 million, respectively, to an escrow account where the funds were held until they were approved for distribution. On June 3, 2020, the Court approved the settlement and entered an order of dismissal. As of the date the condensed consolidated financial statements were issued, the escrow funds have been released and this matter is closed.

#### *LEGAL AND REGULATORY ENVIRONMENT*

The healthcare industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not limited to, matters such as licensure, accreditation, government healthcare program participation requirement, reimbursement for patient services and Medicare and Medicaid fraud and abuse. Government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers.

Violations of these laws and regulations could result in expulsion from government healthcare programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the Company is in compliance with fraud and abuse regulations, as well as other applicable government laws and regulations. While no material regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or unasserted at this time.

#### **Item 1A. Risk Factors**

As disclosed in “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2019, there are a number of risks and uncertainties that may have a material effect on the operating results of our business and our financial condition. The following information updates, and should be read in conjunction with, the factors discussed in Part I, Item 1A, “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2019, which could materially affect our business, financial condition or future results. The risks described in this Quarterly Report and our Annual Report on Form 10-K are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition or operating results.

***We have incurred losses since our inception and expect to incur losses for the foreseeable future. We cannot be certain that we will achieve or sustain profitability.***

We have incurred losses since our inception and expect to incur losses in the future. As of September 30, 2020, we had a net loss of \$8.7 million, negative working capital of \$0.5 million and net cash used in operating activities of \$6.0 million. To date, we have experienced negative cash flow from development of our diagnostic technology, as well as from the costs associated with establishing a laboratory and building a sales force to market our products and services. We

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expect to incur substantial net losses for the foreseeable future to further develop and commercialize our diagnostic technology. We also expect that our selling, general and administrative expenses will continue to increase due to the additional costs associated with market development activities and expanding our staff to sell and support our products.



Our ability to achieve or, if achieved, sustain profitability is based on numerous factors, many of which are beyond our control, including the market acceptance of our products, competitive product development and our market penetration and margins. We may never be able to generate sufficient revenue to achieve or, if achieved, sustain profitability.

Because of the numerous risks and uncertainties associated with further development and commercialization of our diagnostic technology and any future tests, we are unable to predict the extent of any future losses or when we will become profitable, if ever. We may never become profitable and you may never receive a return on an investment in our securities. An investor in our securities must carefully consider the substantial challenges, risks and uncertainties inherent in the development and commercialization of tests in the medical diagnostic industry. We may never successfully commercialize our diagnostic technology or any future tests, and our business may fail.

***We will need to raise substantial additional capital to commercialize our diagnostic technology, and our failure to obtain funding when needed may force us to delay, reduce or eliminate our product development programs or collaboration efforts or force us to restrict or cease operations.***

As of September 30, 2020, our cash balance was \$2.2 million and our working capital was approximately negative \$0.5 million. Due to our recurring losses from operations and the expectation that we will continue to incur losses in the future, we will be required to raise additional capital to complete the development and commercialization of our current product candidates and to pay off our obligations. To date, to fund our operations and develop and commercialize our products, we have relied primarily on equity and debt financings. When we seek additional capital, we may seek to sell additional equity and/or debt securities or to obtain a credit facility, which we may not be able to do on favorable terms, or at all. Our ability to obtain additional financing will be subject to a number of factors, including market conditions, our operating performance and investor sentiment. If we are unable to raise additional capital when required or on acceptable terms, we may have to significantly delay, scale back or discontinue the development and/or commercialization of one or more of our product candidates, restrict or cease our operations or obtain funds by entering into agreements on unattractive terms.

***If we cannot continue to satisfy Nasdaq listing maintenance requirements and other rules, our securities may be delisted, which could negatively impact the price of our securities.***

Although our common stock is listed on the Nasdaq Capital Market, we may be unable to continue to satisfy the listing maintenance requirements and rules. If we are unable to satisfy The Nasdaq Stock Market, or Nasdaq, criteria for maintaining our listing, our securities could be subject to delisting.

On April 29, 2020, we received a letter from Nasdaq notifying us that for the past 30 consecutive business days, the closing bid price per share of our common stock was below the \$1.00 minimum bid price requirement for continued listing on the Nasdaq Capital Market, as required by Nasdaq Listing Rule 5550(a)(2), or the Bid Price Rule. As a result, we were notified by Nasdaq that we were not in compliance with the Bid Price Rule. Nasdaq provided us until December 28, 2020 to regain compliance with the Bid Price Rule.

On June 29, 2020, the Company received a letter from Nasdaq stating that because the Company's shares had a closing bid price at or above \$1.00 per share for a minimum of ten (10) consecutive business days, the Company's stock had regained compliance with the Minimum Bid Price Requirement for continued listing on Nasdaq, and that the matter is now closed.

We are currently in compliance with Nasdaq listing requirements, however, if Nasdaq were to delist our securities, we could face significant consequences, including:

- a limited availability for market quotations for our securities;
- reduced liquidity with respect to our securities;

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- a determination that our common stock is a “penny stock,” which will require brokers trading in our common stock to adhere to more stringent rules and possibly result in reduced trading;
- activity in the secondary trading market for our common stock;
- limited amount of news and analyst coverage; and
- a decreased ability to issue additional securities or obtain additional financing in the future.

In addition, we would no longer be subject to Nasdaq rules, including rules requiring us to have a certain number of independent directors and to meet other corporate governance standards

***We face risks related to health pandemics and other widespread outbreaks of contagious disease, including the novel coronavirus, COVID-19, which could significantly disrupt our operations and impact our financial results.***

Our business could be disrupted and materially adversely affected by the recent outbreak of COVID-19. In December 2019, an outbreak of respiratory illness caused by a strain of novel coronavirus, COVID-19, began in China. As of October 2020, that outbreak has led to numerous confirmed cases worldwide, including in the United States. The outbreak and government measures taken in response have also had a significant impact, both direct and indirect, on businesses and commerce. Global health concerns, such as coronavirus, could also result in social, economic, and labor instability in the countries in which we or the third parties with whom we engage operate.

The spread of COVID-19 has created a worldwide humanitarian and economic crisis. The events we are living through are in many ways unprecedented, with large-scale quarantines, border closings, school closings, and physical distancing. Governments and communities have been jolted into action to “flatten the curve.” As an organization we have accelerated our actions to protect employees, customers and suppliers.

The progression of the outbreak and its effects on our business and operations are uncertain. While we can only estimate the financial impacts to our business, based on current data, we have experienced business interruptions in certain urban markets that continue to range from 30% to 85%. With the understanding that it is extremely difficult to project the full and ongoing impact of state-by-state quarantine and shelter-in-place orders, we anticipate that such rules and restrictions on businesses will continue through the end of 2020 and quite possibly beyond, in various degrees, as the country re-opens state by state, county by county and city by city. Returning to normalcy is conditioned on many factors surrounding the control and or eradication of COVID-19. As such, we are unable to provide additional insight on the impact to our business at this time.

Going forward, we expect that challenges to our business will continue. We have been and will continue to be prudent in managing through this economic crisis. Digital connectivity is now fundamental to the continuity of our business operations. We continually engage our employees and customers in keeping safe. We monitor adherence to governmental guidelines. We have employed remote work where possible. In this uncharted time, we recognize the need for frequent and transparent communication to all parties. As necessary, we will provide additional information related to this economic condition, including the impact to our future operating results due to downturns in global economies and financial markets.

***We face risks related to the Paycheck Protection Program loan (PPP Loan), which could negatively impact our financial position.***

On April 23, 2020, the Company entered into the Promissory Note evidencing an unsecured \$787,200 loan under the PPP. The PPP was established under the recently congressionally-approved CARES Act and is administered by the U.S. Small Business Administration. The PPP Loan to the Company is being made through Webster Bank, N.A.

The term of the PPP Loan is two years. The interest rate on the PPP Loan is 1.00% and payments are deferred for the first six months of the term of the loan. Under the terms of the CARES Act, PPP Loan recipients can apply for and be granted forgiveness for all or a portion of loans granted under the PPP. Such forgiveness will be determined, subject to limitations, based on the use of loan proceeds for payroll costs and mortgage interest, rent or utility costs and the maintenance of employee and compensation levels. The Company intends to use all or a significant majority of the PPP Loan amount for qualifying expenses but no assurance is provided that the Company will obtain forgiveness of the PPP

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Loan in whole or in part. If forgiveness is not granted, the PPP Loan, in whole or in part, will need to be repaid by the Company, which could have an adverse effect on our future cash flows and financial position.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

None.

**Item 3. Default Upon Senior Securities**

Not applicable.

**Item 4. Mine Safety Disclosures**

Not applicable.

**Item 5. Other Information**

None.

**Item 6. Exhibits**

(a) Exhibits

31.1 [Certification of Principal Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, as amended.](#)

31.2 [Certification of Principal Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, as amended.](#)

32.1\* [Certification of Principal Executive Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, as amended.](#)



